Managing risk, enabling trade

December 2018

market monitor

Focus on food performance and outlook

Disclaimer

In this issue...

On the following pages we indicate the general outlook for each sector featured using these symbols:

Excellent
The credit risk situation in the sector is strong / business performance in the sector is strong compared to its long-term trend

Poor
The credit risk in the sector is relatively high / business performance in the sector is below its long-term trend

Good
The credit risk situation in the sector is benign / business performance in the sector is above its long-term trend

Bleak
The credit risk in the sector is poor / business performance in the sector is weak compared to its long-term trend

Fair
The credit risk situation in the sector is average / business performance in the sector is stable

Stable, but susceptible to sudden downside risks

In general, the food sector continues to perform reasonably well, with a stable or even good credit risk situation in many countries. Despite increased uncertainties from rising trade disputes, food markets have so far remained relatively stable, due to generally good supply conditions across most commodities. That said, in the context of heightened food import bills food markets remain vulnerable, with issues such as commodity price volatility, health issues and weather always difficult to predict.

Consumer habits are changing as the end-client increasingly demands full transparency. Widespread distrust has increased the need for food and drink manufacturers to be more transparent about their ingredients, production processes, and supply chains.

Technology is increasingly used to engineer solutions for global food supply. Some forward-looking companies are developing solutions to replace traditional farms and factories with scientifically engineered ingredients and finished products. Developments that engineer food and drink staples such as laboratory-grown meat and animal-free dairy have grabbed headlines, but often the resulting products are expensive, and some are still years away from widespread commercial availability.

Denmark

- A hard Brexit would have a major impact
- Payments take 30-60 days on average
- Mounting problems for smaller players

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months				✔	
Development of non-payments over the coming 6 months			✔		
Trend in insolvencies over the last 6 months			✔		
Development of insolvencies over the coming 6 months			✔		
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance			✔		
Overall indebtedness of the sector			✔		
Willingness of banks to provide credit to this sector		✔			
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months			✔		
General demand situation (sales)			✔		

Source: Atradius

The Danish agro-industrial sector accounts for almost 25% of Danish commodity exports, with more than two thirds of Danish food production destined for export. China has joined Germany, Sweden and the UK as Denmark's most important food export markets, and sales increases in recent years have mainly been driven by demand from emerging markets. The most important export commodities are pigs and pig meat (19%), fish & seafood products (15%), and milk & dairy products (12%).

In general, large Danish food businesses are active globally and performing well, while smaller manufacturing and trading companies supply the domestic market and/or export to close markets like Germany, UK, Sweden and Eastern Europe. Small food producers and wholesalers generally face tough competition and low profit margins.

With its high dependence on exports, free trade and open markets are crucial for the Danish food industry. Current issues in international trade like the Russian import ban and the ongoing US-China trade conflict have a negative impact on Danish food exports. A hard "Brexit" would have serious impacts on the industry, as the UK is one of the most important export markets. It is estimated that a hard Brexit could trigger a significant decrease in Danish export of food and agricultural products to Britain.

Turnover development in the traditional food wholesale and retail segment is rather flat. The domestic market is characterised by excess capacity, fierce competition and price sensitive consumers, putting pressure on retailers´already thin profit margins. The discount segment accounts for more than 40% of the market. Domestic sales of food via retail amounts to EUR 2,300 per capita or approximately 10% of disposable income, which is quite low compared to other European countries. Benefiting from changing consumer habits is catering & food service, which has experienced strong growth in recent years, diverting de-

Denmark : Food and Beverages

	2017	2018f	2019f
GDP growth (%)	2.3	1.5	2.2
Sector value added growth (%)	2.4	0.9	2.9

Average sector growth over the past 3 years (%)	2.1
Average sector growth over the past 5 years (%)	0.9
Degree of export orientation	very high
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

mand away from traditional grocery trade. Online sales of food currently accounts for just 3% of total sales, but is increasing approximately 15% annualy.

Apart from the farming segment and some parts of vegetable production, external financing, including bank loans, is generally quite accessible for food businesses. On average, payments in the Danish food sector take between 30 and 60 days, and the payment experience over the past two years has been good. However, some large players continue to push the supply chain on both price and longer payment terms, adding cash flow challenges to mainly smaller food businesses. The outcome of pricing negotiations, mainly between retailers and smaller food producers, will to a large extent determine the future non-payment and insolvency development in this part of the sector. Payment delays have increased year-on-year in 2018, although from a low level, and are expected to level off in 2019.

Danish food sector

Strengths
High reputation for quality food products
Highly efficient in producing and trading
Good access to external financing sources

Weaknesses
Strongly exposed to international trade issues
Shrinking margins and insufficient investment weaken smaller players
Dependent on commodity price development

Source: Atradius

The insolvency level in the industry is low and the outlook for 2019 is stable. In combination with high gearing and deteriorating prices the summer 2018 draught has led to higher insolvencies among Danish farmers, and this trend is expected to continue in the coming months. However, we expect this to have only marginal effects on other parts of the industry.

For the time being our underwriting approach remains open across all subsectors. However, in the domestic retail businesses fierce competition with price wars have a negative impact on earnings and business stability, mainly for smaller companies. As profit margins are generally low in the food sector, businesses, especially smaller players, are susceptible to sudden market shocks. Therefore we closely monitor the impact of Brexit on food businesses dependent on exports to the UK (mainly seafood, meat and dairy businesses). We also monitor the further developments in the Sino-US trade dispute and assess any negative impact on Danish food exporters.

Performance forecast along subsectors

Beverages	Food manufacturing	Food retail
		

Source: Atradius

France

- Structural weaknesses hamper the sector
- Increasing competitive pressure from EU peers
- Rising payment delays and insolvencies expected in 2019

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months				✔	
Development of non-payments over the coming 6 months				✔	
Trend in insolvencies over the last 6 months				✔	
Development of insolvencies over the coming 6 months				✔	
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance			✔		
Overall indebtedness of the sector			✔		
Willingness of banks to provide credit to this sector			✔		
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months				✔	
General demand situation (sales)			✔		

Source: Atradius

The food industry is a key sector of the French economy, which, according to the National Association of Food Industries (ANIA), generated revenues of EUR 180 billion in 2017, up 3.8% year-on-year. France is the sixth largest food exporter worldwide, with leading positions in segments such as wine, sugar, cheese, and poultry. The French food trade balance generated a EUR 7.5 billion surplus in 2017, up from 7.2 billion in 2016. France enjoys a worldwide reputation for the quality of its food products. However, some structural weaknesses and challenges cast a shadow on the performance outlook.

The increase in the trade balance surplus seen last year is mainly due to both price and volume increases in the beverage segment and higher sugar exports. Along segments, the current trade balance is only positive for beverages, dairy and grain. Excluding beverages there is even a food trade balance deficit, which increased by EUR 0.5 billion last year due to lower meat, fish, fruits, vegetables, animal and vegetable oil exports. The annual deficit for food trade within the EU is deteriorating further as French food processors, particularly in the meat industry, are losing domestic market share due to lack of competitiveness. This is highlighted by a 0.6% decrease in food production in 2017, followed by a 1.1% decrease in H1 of 2018.

Increasingly volatile and rising commodity prices (e.g. for butter, milk or wheat) are a major challenge for French food processors. Many businesses in this segment struggle to pass on higher input prices, which is hampered by the high concentration and market power of retailers and strong competition from other companies within the EU. Margins of food processors have reached an all-time low in 2018, additionally impacted by high labour costs, higher taxation and stricter regulations compared to their foreign competitors. In summer 2017 the French government has initiated a mediation between producers/processors

France: Food and Beverages

	2017	2018f	2019f
GDP growth (%)	2.3	1.6	1.7
Sector value added growth (%)	-0.4	-0.2	1.5

Average sector growth over the past 3 years (%)	0.0
Average sector growth over the past 5 years (%)	0.5
Degree of export orientation	high
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

and retailers with a National Food Conference (Etats Généraux de l'Alimentation), resulting in new rules for annual price negotiations. However, most food manufacturers and syndicates already consider those rules insufficient.

As a whole the French food industry still depends heavily on the domestic market, which accounts for 75% of revenues. Beside the difficulties passing on price increases and losing market shares to foreign peers, French food businesses suffer from the slowed down food consumption growth in France. This is particularly affecting the dairy industry, as sales volumes of all dairy products have been decreasing over the past 18 months. In the meat sector consumption of bovine meats and ham is structurally declining due to health concerns and changing eating habits, while the growing demand for poultry is increasingly met by imports (mainly from Poland).

French food sector

Strengths	The world´s 6th largest food exporter
	High reputation for quality food products
Weaknesses	Some food subsectors are too fragmented
	Shrinking margins and insufficient investment
	High labour costs and strict French hygiene rules affect international competitiveness

Source: Atradius

Given all those difficulties and challenges it comes as no surprise that the portfolio payment experience has been rather bad over the past two years, and both payment delays and insolvencies have increased further in 2018, especially in the meat segment. Increased credit insurance claims both in terms of numbers and value indicate that the French food industry is currently no longer as resilient as it used to be.

In 2019, we do not expect a significant rebound. Most problems are structural, and commodity price volatility has become commonplace as most tariff barriers have been abolished. Moreover, the current international trade disputes and Brexit create significant uncertainty for the French food industry (the food trade surplus with the UK amounted to EUR 5.3 billion in 2017, led by wines, spirits, and dairy products). It is expected that profit margins of French food businesses will decrease further in 2019, while payment delays and insolvencies continue to increase.

Therefore, we have increased our scrutiny on sensitive cases, with more responsive and firm actions for 'grey zone' companies that seem most vulnerable. Overall, we have adjusted our risk acceptance on the weaker segments (especially meat), but maintain a rather neutral underwriting stance on the whole industry. Fraud remains an issue in the French food sector, especially in the wholesale of meat. Fraud detection training for underwriters is a requirement to help them detect suspicious patterns.

Performance forecast along subsectors

Beverages	Food manufacturing	Food retail

Source: Atradius

Germany

- The domestic market situation remains difficult
- Increased payment delays and insolvencies
- Fraud cases are still rising

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months				✔	
Development of non-payments over the coming 6 months			✔		
Trend in insolvencies over the last 6 months				✔	
Development of insolvencies over the coming 6 months			✔		
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance		✔			
Overall indebtedness of the sector			✔		
Willingness of banks to provide credit to this sector				✔	
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months			✔		
General demand situation (sales)			✔		

Source: Atradius

According to the German Food Association BVE, nominal turnover increased 1.1% year-on-year in H1 of 2018, to EUR 88.1 billion, mainly due to slightly higher market prices and sales volumes in Germany and the main export markets.

In 2018 domestic market conditions remained difficult for food producers and processors due to rising input costs, including labour costs, and structurally low margins. The German food retail market is the most competitive in Europe, with low market prices due to the overwhelming power of the leading food retailers and discounters. This, together with tough competition and price wars in the food retail sector indicate that food producers, processors and suppliers have found it difficult to pass on costs. This situation is expected to remain more or less unchanged in 2019.

The situation in the dairy segment has stabilised somewhat since the end of 2016, but volatile market prices and difficulties passing on higher input costs to sales prices remain issues. While overcapacities impact the beverage subsector, many meat processors and producers suffer from higher procurement prices, especially for pork, while their ability to pass on those increases to retailers is limited due to long-term contracts. The introduction of a minimum wage in January 2017 has also contributed to pressure on margins and liquidity, while the market situation is characterised by a surplus supply of standardised meat products.

Food producers and wholesalers pay, on average, within 30 days, while payment terms of food retailers often vary from 45 to 90 or more days. With food processing companies and retailers demanding longer payment terms from their immediate suppliers to improve their working capital, a wave of longer payment terms is being created along the whole supply chain. The already low profit margins are further decreasing for many businesses. While the dependence on banks for external financing is high, financial institutions are rather unwilling to provide loans to food businesses compared to other industries.

Germany : Food and Beverages

	2017	2018f	2019f
GDP growth (%)	2.5	1.8	1.6
Sector value added growth (%)	1.6	1.3	1.5

Average sector growth over the past 3 years (%)	1.0
Average sector growth over the past 5 years (%)	1.4
Degree of export orientation	high
Degree of competition	very high

Sources: Macrobond, Oxford Economics, Atradius

Payment delays and insolvencies have increased slightly, especially in the troubled meat segment, but also in the beverages and fruit & vegetables subsectors. Most at risk to fail are (smaller) businesses that lack export opportunities or that do not offer specialised products, and those companies with already poor financial strength.

Our underwriting stance remains overall neutral to cautious for the food sector, with a more restrictive stance for meat production, meat processing and beverages, as we expect the difficult business environment in those subsectors to continue in 2019.

German food sector

Strengths
Non-cyclical industry
Innovative industry sector reacting to changing consumer behaviour
Profitable export business

Weaknesses
Partial overcapacities
Declining number of consumers and ageing population in Germany
Shrinking margins
Low price levels due to strong discount sector

Source: Atradius

The German food sector remains affected by considerable fraud cases, which are still rising and getting increasingly tricky and professional. Especially in the fish, fruits and vegetables segments criminal buyers order goods easy to resell on credit terms. Therefore, we pay close attention to the number of credit limits that are applied for within a short period, especially where the buyers are recently established and where management and/or shareholders have recently changed or the buyer's business sector does not match with the goods ordered (e.g. a steel company ordering food items). The same accounts when a buyer proactively sends financial figures that indicate unusually high profit margins.

Performance forecast along subsectors

Beverages	Food manufacturing	Food retail
		

Source: Atradius

Italy

- **Growth above 2% expected in 2018 and 2019**
- **Fragmentation and small business size remain an issue**
- **The retail segment remains under pressure**

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months			✔		
Development of non-payments over the coming 6 months			✔		
Trend in insolvencies over the last 6 months			✔		
Development of insolvencies over the coming 6 months			✔		
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance		✔			
Overall indebtedness of the sector		✔			
Willingness of banks to provide credit to this sector		✔			
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months			✔		
General demand situation (sales)			✔		

Source: Atradius

The food sector is one of the most important Italian industries, employing around 385,000 people in more than 6,800 companies, and generating total turnover of more than EUR 137 billion in 2017, which amounts to 8% of Italy´s GDP. Food production increased 3.2% year-on-year in 2017 and 1.9% in 1H of 2018. Export of agrifood products recorded a solid 6.8% increase in 2017, to more than EUR 41 billion, and grew 3.1% in H1 of 2018. Domestic consumption was less dynamic with just a 0.9% increase in 1H of 2018. Italian food production, processing and retail remain heavily fragmented, with a very competitive business environment.

The meat segment has benefited from turnover stabilisation in 2017 and 2018 after several years of declining sales triggered by changed consumption habits, while the beverage sector recorded good export performance, especially for wine. High competition, too many players and a low average size of food retailers impact the food retail segment. Even the biggest Italian food retail businesses are small compared to other major international players. At the same time, e-commerce is increasingly challenging traditional brick-and-mortar food retailers. However, for the time being this segment remains rather resilient, and a positive credit cycle helps mitigate the risk of liquidity distress.

While the general forecast for Italy´s economic performance has become more uncertain, it is expected that food sector growth will continue in 2019, based on the industry´s resilience. While the profitability of food businesses is generally low, profit margins are expected to remain stable in 2019, also taking into account the current level of food raw material prices. Food producers and processors are often highly geared in order to maintain working capital requirements. Due to its anticyclical business performance, lending to the food industry remains appealing to banks and other financial institutions, enabling them to diversify asset investments.

Italy: Food and Beverages

	2017	2018f	2019f
GDP growth (%)	1.6	1.1	0.9
Sector value added growth (%)	0.6	2.0	2.4

Average sector growth over the past 3 years (%)	0.9
Average sector growth over the past 5 years (%)	0.9
Degree of export orientation	high
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

Since 2012 a new law ('Article 62') lays down a maximum payment term in the food sector of 30 days for perishable goods and 60 days for non-perishable goods. We observe that most businesses are abiding by those terms, while requests for protracted payments could be a first signal of liquidity problems of buyers. Given the forecast of solid performance we expect there will be no significant increase in payment delays and/or insolvencies in 2019.

Our underwriting stance for Italian food businesses remains generally open. A more selective approach is applied on the food retailers subsector due to the challenging market environment, including the growing competition from e-commerce.

Italian food sector

Strengths	Non-cyclical sector
	Good reputation of 'Made in Italy'
	Export opportunities
Weaknesses	Many small businesses
	Low capitalisation and tight margins
	High competition

Source: Atradius

As in 2017, we have observed a high degree of suspected frauds in the food sector this year, mainly in the meat, fish and general wholesale segment. Therefore, we take a closer look at the frequency of credit limit applications and the reliability of businesses' management. Financial figures of individual businesses not aligned to average sector/subsector levels serve as a warning sign.

Performance forecast along subsectors

Beverages	Food manufacturing	Food retail
		

Source: Atradius

The Netherlands

- **Robust domestic demand and a good export performance**
- **Payments take 45 days on average**
- **Brexit could become an issue for export businesses**

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months			✔		
Development of non-payments over the coming 6 months			✔		
Trend in insolvencies over the last 6 months			✔		
Development of insolvencies over the coming 6 months			✔		
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance			✔		
Overall indebtedness of the sector				✔	
Willingness of banks to provide credit to this sector		✔			
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months		✔			
General demand situation (sales)		✔			

Source: Atradius

The Dutch food and beverages sector continued to expand in 2018, with value added growth expected to increase by more than 4.5%, and in 2019 more than 2%. Domestic consumption is sustained by continued economic growth and elevated consumer confidence, while export demand has remained robust. The profitability of Dutch food businesses is generally high, and profit margins have increased in 2018, with a stable outlook for 2019.

The domestic food retail subsector continued to grow in 2018, expected to amount to more than EUR 59 billion. Food service (catering, restaurants, leisure, hotels and sales points 'on the move') account for approximately 35% of the total food spending, while the food retail share amounts to about 65%.

The food service segment continues to grow due to the robust economic performance and the fact that people are eating out more often. A rising share of female workers, growing millennial population, busy work schedules, and on-the-go consumption drive this habit. Supermarkets answered this trend by opening shops with a smaller convenience store variety in busy city centres, at train stations and in business parks. Specialty food retail recorded a decline in sales volume in H2 of 2017 and H1 of 2018, not being able to benefit from the overall growth in food expenditure. There is strong competition from supermarket chains, which have further improved their assortment. Therefore, traditional stores have to become specialty shops, pastry and high-end caterers in order to survive in the long-term.

Online food retailing continues gaining momentum. While the market share of online food retail is still small (2.8% in 2017), many indicators show that it will increase sharply in the coming years, up to 9% in 2025. For supermarkets e-commerce is in many cases still loss-making, but also a way to increase market share, bind customers and to keep out new market entrants.

Netherland: Food and Beverages

	2017	2018f	2019f
GDP growth (%)	3.0	2.8	1.7
Sector value added growth (%)	1.2	4.8	2.2

Average sector growth over the past 3 years (%)	2.2
Average sector growth over the past 5 years (%)	2.5
Degree of export orientation	high
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

The Netherlands is one of the world´s largest exporters of agricultural-food products, second only to the US. The meat processing and the dairy industries are the most important sectors within the food export industry.

The business model of the Dutch dairy industry has a very international orientation. Belgium, France and Germany are its main markets within the EU, but markets in Asia and the Middle East are also of major importance. While it is expected that demand for dairy products will increase further in 2019 the operating profits of businesses in the processing industry are under pressure due to low prices for basis dairy products and price competition in infant nutrition in Asia, putting pressure on volume and margins. At the same time Dutch milk supply fell sharply in 2017 and 2018 due to the introduction of a phosphate reduction scheme, as dairy farmers have decreased their number of cows.

Dutch food sector

Strengths	Modern logistics and infrastructure
	Highly efficient in producing and trading
Weaknesses	Price competition with foreign food businesses
	Fierce competition in the retail segment

Source: Atradius

The Netherlands are the largest importer and exporter of poultry meat in Europe. Market conditions in this segment have been favourable, and financial results will exceed the average of the last five years. For the strongly export-oriented veal and beef segment, business conditions are expected to remain stable in 2019. In the pork segment market circumstances have become more challenging due to increased competition and higher raw material costs. A hard Brexit could have major repercussions, as with 14% of volume and 16% of value the UK is the most important market for Dutch pork.

The average payment duration in the sector is 45 days, and the amount of payment delays, protracted payments and insolvencies remains low compared to other Dutch industries, with no major changes expected in 2019. Banks are generally willing to provide loans, while the indebtedness of small and mid-sized Dutch food companies (excluding smaller businesses with less than 10 employees) is low compared to their peers in other EU countries.

Therefore, our underwriting stance remains open for most major food subsectors, while being neutral for speciality retail stores and dairy processing due to the issues mentioned above.

However, risks that could potentially trigger a setback in the sector performance are mounting, as the strong export orientation makes many Dutch food businesses susceptible to geopolitical risks, trade disputes and price/currency fluctuations. Issues like an escalation of the Sino-US trade dispute and a hard Brexit could pose considerable risks in 2019 (e.g. in value added terms, the UK accounts for 8% of Dutch exports and 3% of Dutch GDP).

Performance forecast along subsectors

Beverages	Food manufacturing	Food retail

Source: Atradius

United Kingdom

- High pressure on margins due to increased import costs
- Payments take between 45 and 60 days on average
- Increasing payment delays and insolvencies expected

Overview

Credit risk assessment	significantly improving	improving	stable	deteriorating	significantly deteriorating
Trend in non-payments over the last 6 months				✔	
Development of non-payments over the coming 6 months				✔	
Trend in insolvencies over the last 6 months				✔	
Development of insolvencies over the coming 6 months				✔	
Financing conditions	**very high**	**high**	**average**	**low**	**very low**
Dependence on bank finance		✔			
Overall indebtedness of the sector		✔			
Willingness of banks to provide credit to this sector		✔			
Business conditions	**significantly improving**	**improving**	**stable**	**deteriorating**	**significantly deteriorating**
Profit margins: general trend over the last 12 months				✔	
General demand situation (sales)			✔		

Source: Atradius

The pound sterling depreciation since the June 2016 Brexit decision has increased the costs of commodities and food items for many British food producers and processors reliant on imports (more than 45% of food consumed in the United Kingdom is imported). While the pound sterling exchange rate has been less volatile in 2018 than in 2017, inflationary cost pressure for imported products has remained high.

As a result, input costs for British food businesses remain high, while the chances to pass on price increases to retailers are limited. Further consolidation in the retail segment (especially among large retailers) and the increasing market success of discounters continue to weigh on suppliers along the food supply chain. The leverage against retailers is limited by the fact that the food producer/processing segment is dominated by small and medium-sized players in a highly fragmented market.

As a consequence the profit margins of food businesses deteriorated further in 2018, a development expected to continue in 2019. The trend to low margins and onerous or destabilising contracts remains commonplace in the sector, driven by a need to maintain customer relationships and/or production volumes as a means to cover overheads at the expense of profitability - which is not sustainable in the long-term. Therefore it comes as no surprise that producers and processors are increasingly pursuing mergers and acquisitions in order to increase their leverage in price negotiations (and product offering) with major retailers.

Risk mitigation with forward contracts and currency hedging remains an important discipline for businesses. Undoubtedly, businesses that take forward positions will reduce some of the downside risks associated with pricing and Brexit in general. That said, due to the high share of SMEs in the food producing/processing segment many businesses lack resources and skills/expertise to manage these mechanisms effectively.

United Kingdom: Food and Beverages

	2017	2018f	2019f
GDP growth (%)	1.7	1.3	1.5
Sector value added growth (%)	3.6	1.5	1.0

Average sector growth over the past 3 years (%)	2.0
Average sector growth over the past 5 years (%)	1.9
Degree of export orientation	average
Degree of competition	very high

Sources: Macrobond, Oxford Economics, Atradius

Payments in the British food sector take between 45 and 60 days on average. Due to an inability to absorb higher input costs and increased pressure on margins, both payment delays and insolvencies have increased this year, remaining on a high level. We expect those increases to continue in the first half of 2019, at least. Some larger players continue to push the supply chain on price and longer payment terms, adding cash flow challenges to mainly smaller food businesses.

That said, despite the current difficult trading conditions across the sector, access to external financing (e.g. bank loans) remains reasonably stable. Asset backed lending facilities are extensively used in this sector.

British food sector

Strengths	Resilient, legacy businesses
	Banks remain supportive despite market uncertainty
	Well established, strong global reputation for high food quality and animal welfare standards
Weaknesses	Brexit decision has a major impact in the short and medium term
	Shrinking margins and postponed investments due to unclear outlook
	Poor and extreme weather has interrupted the natural cycle of a lot of domestically grown produce and their respective yields

Source: Atradius

Due to the adverse developments, our underwriting stance has become more restrictive for the food industry in general. This accounts especially for the highly import dependent meat segment, where the weaker exchange rate has added pressure on already thin margins. This subsector is also heavily reliant on agency workers, the availability of which has reduced sharply. This has in turn pushed up labour costs. A hard Brexit scenario would pose a material threat to this subsector. We are also rather restrictive with the fruit/vegetables segments, as this subsector is highly dependent on imports too. The levels of both short firm fraud and impersonation fraud have remained stubbornly high in 2018, mainly in the meat and fruit/vegetables subsectors, and no improvement is expected in 2019.

We are also more cautious with the dairy segment, where movement in farm gate prices and adverse weather conditions in 2018 have negatively impacted margins and further increased pressure across the supply chain. Fixed price contracts mean producers and processors are not necessarily able to recoup their margins.

Due to reasonably good performance and robust export sales in some segments (e.g. liquors) our underwriting stance remains neutral for the beverages subsector, while we remain generally open for food retail. However, the increasing success of discounters is driving structural change within this segment, hence there is significant consolidation in the market. (e.g. Tesco's merger with Booker and the potential merger between Asda and Sainsbury´s).

We maintain frequent contact with companies within the sector allowing us to remain very close to developments in the industry and vigilant to changing dynamics and challenges throughout the food supply chain. The fact that we are in contact and receive management accounts of many food companies means that we are able to continue to write limits and maintain an acceptable risk appetite.

Performance forecast along subsectors

Beverages

Food manufacturing

Food retail

Source: Atradius

Market performance at a glance

Australia

- Australian food production has grown steadily over the past couple of years. Key drivers have been population and income growth as well as changes in tastes and preferences.
- That said, higher input costs have increased pressure on margins in recent years, with a recent draught in Australia having and additional negative impact. In 2019 food businesses profit margins are expected to decrease further. Price wars are fairly common in the food retail sector, where bigger players compete for market share by pushing prices down. This causes tighter margins for producers. As a consequence mergers and acquisitions are ongoing amongst food producers in order to achieve economies of scale.
- While the gearing of food businesses is generally high, financing conditions in the industry are good as the agrifood sector is one of the main contributors to GDP in Australia. Banks are generally willing to provide loans to the industry.
- The number of non-payment notifications in the sector has increased in 2018, and is expected to rise further over the next 6 months. As the drought situation in Australia has put additional pressure on the margins of players across the industry due to higher input costs, many businesses are struggling to breakeven, and some have even incurred losses. That said, the insolvency environment is expected to remain stable, with no major increase expected.
- Our current underwriting stance remains generally open, while we monitor the future impact of the current draught on the industry. We are very open for the beverages segment, which mainly consists of well-established players with solid financials. We remain open for food retail, despite lower profit margins and fierce competition, as demand will remain high.
- Our underwriting stance is generally open to neutral for businesses in the dairy segment. Demand is expected to remain high, especially for infant formula milk in Asia (mainly China), but market conditions are volatile.
- As food traders and wholesalers are very susceptible to commodity price changes and the subsequent impact on margins, we usually have a more conservative strategy on those players.
- The meat sector is restrictively underwritten due to tight supply, high prices and increased input costs, triggered by the current drought situation on the Australian East coast. We are very restrictive with buyers engaged in pork processing due to a plunge in farm gate prices at the start of 2018 to a level where farmers were struggling to break even. If the adverse weather conditions continue, we expect the performance of buyers active in the meat segment to deteriorate further.

Australia: Food and Beverages

	2017	2018f	2019f
GDP growth (%)	2.2	3.3	2.6
Sector value added growth (%)	4.8	3.2	6.2

Average sector growth over the past 3 years (%)	1.2
Average sector growth over the past 5 years (%)	0.8
Degree of export orientation	high
Degree of competition	very high

Sources: Macrobond, Oxford Economics, Atradius

Performance forecast along subsectors

Beverages	Food manufacturing	Food retail
		

Source: Atradius

Ireland

- The agri-food and beverages sector accounts for about 8% of Ireland's economy, more than 10% of its exports and about 8% of total employment. The total value of the Irish food and drink industry amounted to EUR 26 billion in 2017, of which EUR 13.6 billion was exported (up 13% year-on-year).
- All main subsectors have performed rather well over the past two years. Meat processors have benefited from robust domestic and export demand, including higher sales to Asia in 2018. The dairy segment has increased milk powder sales in new overseas markets, while the highly competitive domestic food retail market has benefitted from robust and growing consumer demand.
- In 2017 sales to the UK accounted for 35% of exports (down from 37% in 2016 and 41% in 2015), while other EU markets accounted for 33%. The pound sterling depreciation against the EUR after the June 2016 Brexit referendum had negative consequences for many exporters. Meanwhile Irish businesses have started to diversify by increasing their market share in mainland Europe, although that happens at low margins.
- Despite the efforts of food exporters to diversify shipments away from Britain, a hard Brexit remains a major threat to the sector. Any future imposition of tariffs by the British government on food imports from the EU after leaving could be devastating for the Irish food sector (e.g. exports of cheddar cheese to the UK, valued at over EUR 300 million, would face a 55% tariff).
- A hard Brexit could also cause delays in shipments of fresh food to Europe, increasing cost and reducing competitiveness (almost 80% of Irish exports to Europe pass via the UK). Shipping live animals between the Republic of Ireland and Northern Ireland would also become an issue.
- In order to counteract the threat of tariffs in the event of a hard Brexit, Irish companies have continued to acquire smaller UK operators in order to maintain access to the UK market after Brexit. Additionally a consolidation process among smaller Irish food businesses is ongoing.
- The average payment duration in the Irish food industry is 45 days. Payment behaviour in the sector has been very good over the past 12 months, and the number of protracted payments, non-payments and insolvency cases is still low. Therfore, our sector performance assessment still remains "good" for the time being.
- However, as the Irish food sector will remain exposed to further currency volatility and growing risks in relation to the decision of the United Kingdom to leave the EU, we expect both payment delays and insolvencies to increase in 2019.

Ireland: Food and Beverages

	2017	2018f	2019f
GDP growth (%)	7.3	6.1	2.5
Sector value added growth (%)	7.0	4.1	2.0

Average sector growth over the past 3 years (%)	8.2
Average sector growth over the past 5 years (%)	7.5
Degree of export orientation	very high
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

Performance forecast along subsectors

Beverages	Food manufacturing	Food retail

Source: Atradius

Mexico

- The Mexican food industry has performed well in 2018, with total sales expected to increase 8.7% year-on-year, to MXN 1,810 billion (EUR 78.7 billion). The Mexican food and agriculture sectors are highly export-driven, and most businesses showed stable profit margins in recent years as the United States kept zero duty for all Mexican imports in line with the NAFTA agreement. According to the draft of the renegotiated USMCA agreement, all current zero tariffs for food and agricultural products under the NAFTA will remain unchanged.
- However, the USMCA agreement is still subject to ratification in all three member states. Should this fail and trade disputes flare up again it could have a major impact on the industry, as Mexican food and agriculture exports to the US could be impacted by tariffs. At the same time Mexico imports most of its dairy from the US, and another deterioration of the US-Mexican trade relationsship could encourage Mexico to boost production at home.
- Mexico's food sector could see some significant structural changes with the inauguration of President Andrés Manuel López Obrador. The new government could launch policies to increase domestic production and put emphasis on domestic agricultural support programmes. Currently Mexico still imports over 40% of the food it consumes, predominantly from the US, and runs a trade deficit in dairy, livestock, grains and oilseeds.
- Financing requirements and financial gearing are high in the food industry, and the willingness of banks to provide loans has encouraged further investments. The maximum payment period ranges from 30 to 120 days depending on the kind of products (perishable or non-perishable food products).
- Payment delays could increase in the coming months due to ongoing market uncertainty over the future of USMCA. However, at the same time the new administration's pledge to raise the minimum wage and boost living standards across the population augurs well for growth prospects in the food and drink industry. The insolvency level in the food industry is generally low, and no major increase is expected in 2019. Most of overdue payment is due to administrative reasons or commercial disputes, mainly covering small amounts.
- For the time being our underwriting stance for the food sector remains generally open for all main subsectors. The outlook for meat, dairy, beverages and food retail is positive, with steady sales growth expected in the short- and medium-term. For small buyers we try to obtain updated financial information and put emphasis on healthy financial ratios, low leverage profile and low risk concentration. We will carefully monitor the further USMCA process and adapt our underwriting stance if necessary.

Mexico Food and Beverages

	2017	2018f	2019f
GDP growth (%)	2.3	2.0	2.2
Sector value added growth (%)	1.9	2.8	2.2

Average sector growth over the past 3 years (%)	2.6
Average sector growth over the past 5 years (%)	1.8
Degree of export orientation	very high
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

Performance forecast along subsectors

Beverages	Food manufacturing	Food retail

Source: Atradius

Poland

- The food sector is one of Poland's strongest industries, accounting for 13% of GDP in 2017. The sector is developing well as a result of growing domestic and export demand.
- Competition in the Polish food market is high, especially on price. While profit margins for most businesses are stable, they generally remain at a low level. Higher profits are only generated by larger entities or small specialised players, while many smaller and mid-sized businesses struggle to perform well. Therefore it comes as no surprise that a consolidation process has started in this segment and smaller players are seeking investors.
- Financing requirements and financial gearing are high in the food industry. After Poland´s EU accession food producers made major investments in order to improve their competitive stance in the European market, mainly provided by bank financing. The currently low interest rates and the willingness of banks to provide loans have encouraged further investments. However, difficulties in repaying bank loans could increase should interest rates rise again.
- The average payment duration in the Polish food industry is 30 days. The number of protracted payments is generally high, as larger businesses use their leverage against suppliers by demanding long payment terms or prolong payments in order to improve their own cash flow. The level of non-payment notifications is high and has increased in 2018, but it is expected that it will decrease in the coming months. The insolvency level is average compared to other industries, and no major increase is expected in 2019.
- Our underwriting varies by subsector. It is mainly neutral for the meat subsector, where the poultry segment is generally doing well, while pork is affected by the closure of several overseas markets due to the African Swine Fever (ASF). The meat segment will benefit from large investments made by big international players.
- We are open for Polish dairy businesses as this segment is currently doing well, and neutral for beverages, where price competition is an issue.
- That said, we are restrictive for food retail, especially for medium-sized players, as many of them work on tiny or even negative margins due to fierce price competition in a domestic market with very price-sensitive consumers.
- Fraudulent events are a concern in both domestic and export business transactions throughout all food subsectors, but most prominent in the fruit & vegetables and meat segments.

Poland: Food and Beverages

	2017	2018f	2019f
GDP growth (%)	4.6	4.6	3.2
Sector value added growth (%)	4.0	4.4	3.5

Average sector growth over the past 3 years (%)	3.2
Average sector growth over the past 5 years (%)	2.1
Degree of export orientation	high
Degree of competition	high

Sources: Macrobond, Oxford Economics, Atradius

Performance forecast along subsectors

Beverages	Food manufacturing	Food retail

Source: Atradius

United States

- Food and beverage processing and manufacturing is one of the largest US industries in terms of employment, providing jobs for about 1.5 million workers annually. The sector consists of approximately 21,000 companies, and value added is forecast to grow 4% in 2018 and 2.2% in 2019.
- Competition is fierce in all main segments along the value chain (manufacturers, retailers, distributors), which has an adverse effect on businesses profit margins. After shrinking in 2018 profit margins are expected to decrease further in 2019, as fuel prices and other input costs are increasing.
- There have been many mergers and acquisitions (M&A) over the last couple of years, signaling a trend towards greater consolidation among large and legacy food brands. M&A activity will remain high as companies continue to look for sales growth and margin improvement. Success will depend on the ability of businesses to optimise synergies and to integrate smoothly.
- Organic food sales in the US still amount to just 5% of overall food sales, but have increased in recent years and are expected to grow further above the average market growth rate. Food preferences of consumers continue to benefit grocery stores where packaged food manufacturers have less of a presence. Natural, organic and gluten-free foods are strategic areas for companies aiming to increase sales growth. At the same time, new regulatory standards will play a significant part in determining food demand.
- The average payment duration in the US food industry is 30 days. Non-payment notifications remained stable in 2018, and we expect no increase in 2019. Additionally, no insolvency increase is expected next year. Access to external financing is not an issue, but many food businesses are private equity-owned and therefore highly leveraged.
- Our underwriting stance is generally open for the beverage segment and neutral for food manufacturing. However, we are more restrictive with food retail, due to throat-cutting competition, slow growth of legacy retailers and extremely tight margins in this subsector.
- As food safety and sustainability are becoming increasingly important, business success depends on the strength and transparency of the supply chain. Foodborne illnesses, contamination and fraud remain risks for food manufacturers - with a potentially major negative effect on profitability.

United States: Food and Beverages

	2017	2018f	2019f
GDP growth (%)	2.2	2.9	2.5
Sector value added growth (%)	4.0	4.0	2.2

Average sector growth over the past 3 years (%)	3.1
Average sector growth over the past 5 years (%)	2.6
Degree of export orientation	high
Degree of competition	very high

Sources: Macrobond, Oxford Economics, Atradius

Performance forecast along subsectors

Beverages	Food manufacturing	Food retail
		

Source: Atradius

Industries performance forecast per country

December 2018

	Agriculture	Automotive/ Transport	Chemicals/ Pharma	Construction Const.Mtrls	Consumer Durables	Electronics/ ICT	Financial Services
Austria	⛅	🌧	⛅	⛈	☁	☁	☀
Belgium	☁	☁	☀	🌧	☁	⛅	☁
Czech Rep.	⛅	☁	⛅	🌧	☁	☁	⛅
Denmark	⛈	☁	⛅	☁	🌧	☁	☁
France	🌧	☁	☀	🌧	☁	☁	⛅
Germany	☁	☁	☀	☁	☁	☁	⛅
Hungary	☁	☁	⛅	☁	☁	☁	☁
Ireland	☁	☁	⛅	⛅	☁	⛅	⛅
Italy	⛅	⛅	⛅	⛈	🌧	⛅	⛅
The Netherlands	⛅	☁	☀	⛅	☁	⛅	⛅
Poland	☁	🌧	☁	🌧	🌧	🌧	⛅
Portugal	☁	☁	🌧	🌧	☁	☁	🌧
Russia	🌧	☁	🌧	🌧	☁	🌧	☁
Slovakia	☁	⛅	⛅	🌧	☁	☁	⛅
Spain	☁	☁	⛅	🌧	☁	☁	☁
Sweden	⛅	☁	⛅	🌧	⛅	⛅	⛅
Switzerland	⛅	☁	⛅	🌧	☁	☁	☀
Turkey	⛅	⛅	☁	⛈	☁	🌧	⛅
UK	🌧	☁	⛅	🌧	🌧	☁	☁
Brazil	☁	🌧	☁	🌧	⛈	⛈	⛅
Canada	☀	☁	☁	☁	☁	☁	☀
Mexico	☁	⛅	☁	🌧	☁	☁	⛅
USA	☁	☁	⛅	☁	☁	⛅	⛅
Australia	⛅	🌧	☁	🌧	☁	⛅	⛅
China	☀	☁	☁	🌧	☁	☁	☀
Hong Kong	☁	☁	☁	☁	☁	⛅	⛅
India	☁	☁	⛅	🌧	☁	☁	☁
Indonesia	☁	☁	☁	☁	☁	☁	⛅
Japan	⛅	☁	☁	☁	☁	⛅	⛅
New Zealand	⛅	🌧	⛅	⛅	🌧	⛅	⛅
Singapore	⛅	🌧	☁	🌧	☁	☁	⛅
Taiwan	☁	🌧	☁	☁	⛅	⛅	☁
Thailand	☁	⛅	☁	☁	☁	☁	⛅
United Arab Emirates	⛅	☁	☁	🌧	🌧	🌧	⛅

Food	Machines/ Engineering	Metals	Paper	Services	Steel	Textiles
Good	Good	Fair	Fair	Good	Poor	Poor
Good	Fair	Fair	Poor	Poor	Good	Poor
Good	Good	Fair	Fair	Fair	Fair	Poor
Good	Fair	Fair	Bleak	Fair	Poor	Poor
Fair	Fair	Fair	Poor	Fair	Fair	Poor
Fair	Good	Fair	Poor	Good	Fair	Poor
Fair	Good	Poor	Fair	Good	Poor	Poor
Good	Fair	Fair	Bleak	Fair	Fair	Poor
Good	Excellent	Fair	Fair	Fair	Fair	Poor
Excellent	Good	Good	Fair	Good	Fair	Fair
Fair	Poor	Fair	Fair	Good	Fair	Fair
Fair	Fair	Poor	Poor	Good	Poor	Poor
Fair	Bleak	Fair	Fair	Poor	Fair	Fair
Good	Good	Fair	Fair	Fair	Fair	Poor
Good	Fair	Fair	Poor	Good	Fair	Poor
Good	Good	Poor	Fair	Fair	Poor	Poor
Good	Good	Fair	Fair	Good	Poor	Fair
Good	Fair	Bleak	Poor	Poor	Fair	Poor
Poor	Fair	Fair	Poor	Poor	Fair	Poor
Good	Poor	Poor	Fair	Fair	Poor	Poor
Good	Fair	Fair	Poor	Good	Fair	Bleak
Good	Fair	Poor	Good	Good	Poor	Poor
Good	Fair	Fair	Poor	Good	Fair	Fair
Good	Fair	Poor	Poor	Fair	Poor	Poor
Good	Fair	Bleak	Poor	Good	Bleak	Poor
Excellent	Fair	Poor	Fair	Good	Poor	Fair
Good	Fair	Poor	Good	Good	Poor	Fair
Good	Fair	Poor	Fair	Fair	Poor	Fair
Good	Fair	Fair	Fair	Good	Fair	Poor
Fair	Fair	Fair	Poor	Poor	Poor	Poor
Good	Fair	Fair	Fair	Good	Poor	Fair
Excellent	Fair	Poor	Fair	Good	Poor	Fair
Good	Fair	Fair	Fair	Fair	Poor	Bleak
Poor	Fair	Poor	Fair	Good	Poor	Poor

Excellent

Good

Fair

Poor

Bleak

Industry performance

Changes since November 2018

Europe

Italy

Construction

Down from Poor to Bleak

The sector suffers from a negative outlook for public investments and a significant insolvency increase of larger players.

Consumer Durables

Down from Fair to Poor

The industry is impacted by stressed market conditions, high competition, lower consumption and a negative market outlook. Within the sector medium-sized larger retailers have started to suffer from increased liquidity tensions.

United Kingdom

Agriculture

Down from Fair to Poor

Increased feed and energy costs adversely affect sector performance, while lingering uncertainty over the final Brexit outcome and the future trade relations with the EU have dampened business sentiment.

Food

Down from Fair to Poor

See article on page 15.

Consumer Durables

Down from Fair to Poor

Services

Down from Fair to Poor

Both sectors are impacted by increased economic uncertainty, lower GDP growth prospects and decreased consumer confidence.

If you've found this report useful, why not visit our website www.atradius.com, where you'll find many more Atradius publications focusing on the global economy, including more country reports, industry analysis, advice on credit management and essays on current business issues.

On Twitter? Follow @Atradius or search #marketmonitor to stay up to date with the latest edition

Connect with Atradius on Social Media

@atradius Atradius atradius

Atradius N.V.
David Ricardostraat 1 · 1066 JS Amsterdam
Postbus 8982 · 1006 JD Amsterdam
The Netherlands
Phone: +31 20 553 9111

info@atradius.com
www.atradius.com