

COMMERCIAL BANKING



Bank of Scotland Food and Drink Report

Executive Summary



**BANK OF
SCOTLAND**

Foreword



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Scotland's food and drink industry helps to define us as a nation.

It contributes more than £1.9bn to our economy¹, has a turnover of more than £14bn² and employs more than 119,000 people³. It is our largest manufacturing sector. And it has a global reputation for quality, which is why our longstanding support for the sector is a point of pride for Bank of Scotland.

This year our survey of 100 Scottish food and drink firms found an industry that retains great pride in the provenance of its produce.

The sector is seeking new opportunities to trade, build and grow overseas, and has ambitious plans to create more than 18,000 new jobs over the next 5 years.

It is an ambitious sector, with plans led by Scotland Food and Drink to grow to £30bn by 2030.

And, it is facing up to challenges around access to labour and boosting productivity through investment and innovation.

This report is a snapshot of an industry that remains robust in the face of economic and political uncertainty, and I hope you find it both insightful and inspiring.

1 Scotland Food and Drink Federation, Statistics at a Glance

2 Scottish Government, Growth Sector Briefing - Food and Drink

3 Skills Investment Plan, For Scotland's food and drink sector

▶ **The Scottish food and drink sector has strong investment intentions and ambitious plans for growth, and our research has revealed a sector more determined than ever to trade, build and grow.**

Growth

Firms' forecasts for growth in the next five years remain robust given the prevailing environment at 21% of current annual turnover (down slightly from 24% last year).

Investment plans have remained steady, with firms saying they plan to invest 59% of their current annual turnover in their business over the next five years.

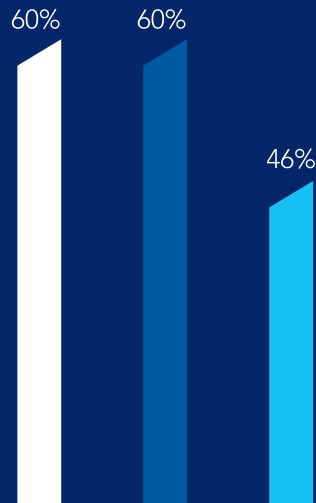
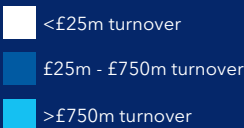
That's up on 56% last year and 40% in 2015, and higher than the average 52% seen across the UK as a whole.

Despite the sector enjoying record exports last year, entering new markets in the UK remains the most popular route to growth (up from 49% last year to 68%), followed by job creation (up from 36% to 54%) and new product development (up from 45% to 54%).

Plans to drive growth through the development of existing products have also grown (up from 34% to 46%), as has investment in infrastructure (from 29% to 38%).

Even in the current low interest rate environment, the most popular ways to fund growth are via making efficiencies through cost savings (54%), cash flow/working capital finance (up from 30% in 2016 to 46%) and cash reserves (up from 35% to 41%).

How much, as a percentage of current turnover, are you planning to invest in your business over the next five years?



Employment

Scottish food and drink firms clearly believe that headwinds are growing when it comes to recruitment, likely to be because of the industry's reliance on EU workers.

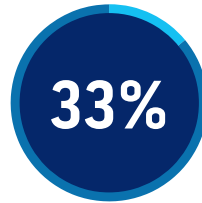
Rising labour costs were flagged by 44% as the biggest challenge to the industry in the next five years, growing from 28% last year and leapfrogging concerns about leaving the EU to become the sector's primary challenge.

The number of firms flagging a lack of skilled labour as a challenge also grew; from a quarter (25%) to a third (33%).

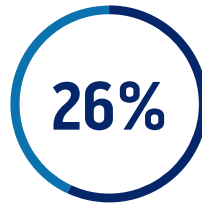
When asked if recruitment plans had been affected by the UK's planned exit from the EU, 67% say yes.

Despite these challenges, the sector's plans to create new jobs have increased year-on-year. Firms in Scotland plan to create 18,200 new jobs over the next five years, up from 14,300 this time last year.

And employers are still investing in their staff. The number of firms investing in skills development in order to make their business more productive grew from 31% to 45%.



said availability skills was a significant labour challenge to the industry in the next five years



said the Living Wage increase was a challenge for the industry

► **“The need to protect trade with Europe and attract value and skills from overseas is central to unlocking our potential”**

James Withers, Scotland Food and Drink

Industry Focus — The supply chain

The current negotiations over the UK's departure from the EU raise important questions about how food and drink firms' supply chains will be affected.

For Scottish firms, leaving the EU remains the biggest threat to ingredients/supply security in 2017, cited by 44% of firms.

And concerns about ingredient price volatility challenges have increased for a significant minority, doubling from 18% to 36%.

That said, agricultural price volatility has so far benefitted more firms than it has hindered, with 42% claiming a positive impact on their business, compared to 23% reporting a negative impact and 35% no effect.

But half (50%) of the Scottish firms surveyed said the UK's planned exit from the EU had already caused them to import less raw materials.

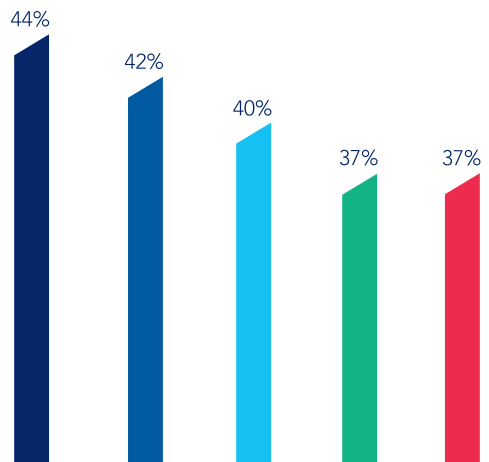
This trend could help boost the Scottish supply chain going forward, with 62% saying they would be prepared to pay a higher price to primary producers based on home turf in order to guarantee security of supply and maintain the provenance of their products.



said they are importing less raw materials because of the UK's planned exit from the EU

Which of the following are the biggest threats to ingredient/supply chain security in the next five years?

- Rising labour costs
- Leaving the EU
- Sugar levy
- Overseas competition
- Sustainability of supply chain



Challenges and Opportunities

Boosting productivity is key to the UK government's growth strategy, and impressive progress has been made north of the border, with figures from the Scottish government showing Scottish productivity has now effectively caught up with UK levels⁴.

Scottish firms appear convinced of the benefits of boosting their productivity further, with 72% making efficiency savings in order to make their business more productive, up from 40% last year.

Other popular productivity strategies are stream-lining processes (63%), investing in new technology (46%) and investing in skills development (45%).

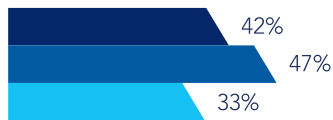
Firms told us that an average 36% of their processes were currently automated, but expected that to rise to 53% in the next five years, with 44% saying they planned to invest more in automation in the coming year.

And 57% said they would be investing in improving digital technology within their business.

Amid this entrepreneurial activity, it was perhaps surprising to see a small decline in the amount of investment being ringfenced for R&D in the next five years, which fell from 39% to 35% of turnover.




⁴ Scottish Government, Scottish productivity growth four times faster than UK, 15 February 2017

Percentage of firms that plan to invest more in automation over the next 12 months



What percentage of your processes do you expect to be automated in the next five years?



-  <£25m turnover
-  £25m - £750m turnover
-  >£750m turnover

International expansion

The value of sterling should continue to boost competitiveness overseas during 2017, supporting the 36% of firms that plan to enter new EU markets, and the 26% targeting new markets outside the EU.

Currently, just one in five UK food and drink companies is an exporter⁵, so it is heartening to see 21% of Scottish firms saying they plan to grow by exporting for the first time, rising to 31% among SMEs.

Firms have continued confidence that their produce has a good reputation internationally, a view held by 96% of businesses, and they harbour growing plans to enter major markets around the world.

Western Europe remains the main target (up from 48% in 2016 to 61%), followed by South America (up from 32% to 57%), the Middle East (up from 31% to 44%), North America (up from 38% to 49%) and the Far East/Asia (up from 31% to 33%).

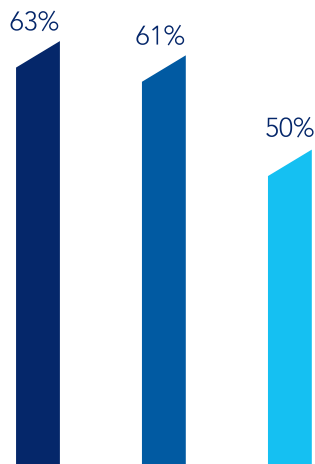
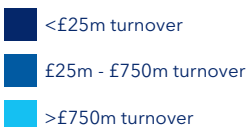
But respondents flag a number of barriers to international trade, chiefly complexity of logistics and UK political uncertainty (both 64%), cash flow (50%), and domestic regulation (50%).

⁵ UK Food and Drink International Action Plan 2016-2020

► **“It is great to see that our Scottish food and drink businesses remain hugely ambitious, with 61% looking to develop in new markets”**

James Withers,
Scotland Food and Drink

Percentage of firms planning to engage new international customers in the next five years.



The Support You Need



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Methodology:

Field research for this report was undertaken in July 2017 by Coleman Parkes Research.

To gather representative data, a cross section of 100 food and drink businesses in Scotland were interviewed. Companies ranged in size, from less than £25m (SME), to between £25m and £750m (Mid market), and more than £750m (Global corporates) annual turnover.

Reference:

- 1 - Scotland Food and Drink Federation, Statistics at a Glance
- 2 - Scottish Government, Growth Sector Briefing - Food and Drink
- 3 - Skills Investment Plan, For Scotland's Food and Drink sector
- 4 - Scottish Government, Scottish productivity growth four times faster than UK, 15 February 2017
- 5 - UK Food and Drink International Action Plan 2016-2020

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