Atradius

Managing risk, enabling trade

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market monitor

Focus on food performance and outlook

Disclaimer

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


Excellent


Good


Fair


Poor


Bleak

Food for thought

In many markets exports clearly play an essential role in the profitability of the food sector, sometimes compensating for less positive results in the home market. Overall the bargaining power of major retailers and discounters has been growing, making life increasingly difficult for many of their suppliers whose margins are becoming stuck at low levels or even shrinking.

Lower commodity prices have provided some relief for food producers and processors since 2014. Within the EU food market the competition between European food businesses is increasing, with efficiency and low production costs being key strengths for sustaining a competitive edge.

The impact of Russia's ban on imports of food from the EU has been felt by some subsectors (especially dairy and fruits and vegetables). While seriously affecting Russian food importing businesses, it has so far not led to severe repercussions or sharply increasing payment delays and insolvencies for EU food companies. In many cases businesses were able to find alternative export markets.

In general, the food sector is currently performing reasonably well, with a rather stable credit risk situation in many countries. However, given that profit margins of many companies are small, the food sector remains susceptible to downside risks, such as volatile commodity prices, sudden economic downturns and health issues.

Belgium

- **High growth of overseas food exports**
- **Margins under pressure due to high labour and energy costs**
- **Still a cautious underwriting approach**

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 Belgian food sector recorded modest turnover growth of 0.3% in 2014, reaching EUR 48.3 billion. Companies active in the food segment increased their investment by 11.9%, to a record EUR 1.3 billion. When taking into account direct and indirect jobs, the Belgian food sector employs 187,000 people and increased its share in the Belgian manufacturing industry to 17.7% in 2014.

Food exports grew 2.1% in 2014, resulting in a positive trade balance of EUR 3.9 billion, which increased 11.8% compared to last year. While France, the Netherlands and Germany still account for the largest share of total exports (57%), deliveries to overseas markets recorded a whopping increase of 12.5%. Very large increases were recorded for exports to the US (up 17.4%), Brazil (up 31.9%) and China (up 23.6%). Subsectors with the strongest export performance are meat, dairy, fruit & vegetables, cereal and beverages. Quality and safety standards as well as process and product innovation are key selling points abroad. The Belgian food sector also excels with organisational and marketing innovations. Exports are expected to increase further in 2015, creating more jobs in the industry.

However, the Belgian food sector also faces some challenges that hamper its performance: besides high energy costs, which mainly affect smaller businesses, the food sector has difficulties in hiring staff with dedicated skills required in the industry (e.g. technicians, machine operators). At the same time, labour costs are more than 20% higher than in France, Germany and the Netherlands, countries which host big competitors. This has had a negative effect on the profit margins of many Belgian food businesses. That said, the recent boost in investments should help ensure that the food sector increases its productivity, helping it cope with mounting price pressure from high domestic labour and energy costs.

Belgian food companies have been facing declining raw materials prices since 2014. While this has negative consequences

Belgium: Food and beverages sector

	2014	2015f	2016f
GDP growth (%)	1.1	1.3	1.7
Sector value added growth (%)	0.3	1.5	1.2

Sector share in the national economy (%)	2.2
Average sector growth over the past 3 years (%)	0.0
Average sector growth over the past 5 years (%)	1.2
Degree of export orientation	high
Degree of competition	high

Sources: IHS, Atradius

for farmers and growers, it creates opportunities for processing companies. It is however vital to hedge against such price swings in order to reduce risk on the already narrow margins.

The food sector has seen a slight improvement in non-payments and insolvencies (84 insolvency cases between January and September 2015, compared to 88 cases in the same period of 2014). It is expected that the level of payment delays and insolvencies will remain stable in the coming six months.

Despite continued growth in the food sector, our underwriting stance remains generally cautious. The meat subsector suffers from margin pressure and high competition, while a consolidation process is on-going in this segment. Some meat exporters are negatively affected by the Russian food import ban, which has also increased pressure on the fruit and vegetables segment.

Milk prices have decreased as a result of the abolition of EU milk quotas, and this will probably have a negative effect on producers, while being an advantage for processors.

We take into account the seasonal trends that affect most food subsectors and manage credit exposure through time-limited cover. Despite our generally cautious stance, we try to find ways to provide cover by obtaining additional information, for instance, good payment experience or a guarantee from a stronger parent company.

Belgian food sector

Strengths	Located in the centre of Western Europe
	High quality of food products
	Strong export performance
Weaknesses	High labour costs
	High energy costs
	Lack of skilled staff

Source: Atradius

France

- The meat and dairy subsectors still face challenges
- Payments are often up to 15 days overdue
- Production costs remain too high

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 National Association of Food Industries (ANIA), turnover of the French agri-food industry decreased 1.8% in 2014, to EUR 157.6 billion, while production declined 0.5% in volume and 1% in value. The sluggish French economic performance still hinders a robust rebound in consumer spending, therefore negatively affecting margins of industrial food manufacturers. While commodity price decreases in 2014 and H1 of 2015 (e.g. for wheat, milk and vegetables) have helped food producers to temporarily rebuild margins, this effect was mitigated by the fierce price competition in the French retail segment and contractual price-adjustment mechanisms. The on-going concentration process of retail chains has further weakened the bargaining power of food producers and processors, who are at the same time in competition with other European food businesses which in some cases have lower production costs. Still, the French agri-food industry is struggling with rising production costs, while gross margins have decreased for several years. This limits investments by businesses, that could increase their international competitiveness.

According to the French Ministry of Food and Agriculture (AGRESTE), food production (including beverages) rebounded 1% in Q2 of 2015. The industry has benefited from falling raw material prices and a weaker euro, which helped boost competitiveness abroad. In H1 of 2015 the food trade balance remained positive.

Payments in the French food industry can be overdue up to 15 days. A slight increase of non-payment notifications cannot be ruled out in the coming months, as some food businesses may face little support from their banks. Generally, French food businesses are highly dependent on bank finance, and many companies have high short-term debts to finance their working capital requirements.

France: Food and beverages sector

	2014	2015f	2016f
GDP growth (%)	0.2	1.1	1.3
Sector value added growth (%)	0.0	0.5	1.2

Sector share in the national economy (%)	1.8
Average sector growth over the past 3 years (%)	-0.9
Average sector growth over the past 5 years (%)	0.4
Degree of export orientation	high
Degree of competition	high

Sources: IHS, Atradius

In H1 of 2015 food business insolvencies rose 0.9%, mainly due to an increase in the bakery segment. Without the increase in this segment, the food insolvency rate would have improved. In Q3 of 2015 food insolvencies decreased slightly, by 0.8%. This is in contrast to the overall French business insolvency development, where insolvencies are expected to increase 4% in 2015. However, due to some problems in the dairy and meat subsector, an insolvency increase in the coming six months cannot be ruled out.

Dairy products form the second largest food industry subsector, accounting for 17% of total food sales. International milk powder and butter prices have already fallen for several months, and this downward trend has accelerated in 2015 due to fewer Chinese imports and the Russian import ban which is still effective. While lower prices have been beneficial for cheese manufacturers, exports of milk powder have been severely impacted. Some main players have invested large amounts in expanding their production capacities before demand from China decreased. If this subdued demand situation persists, it could lead to cash flow and debt repayment issues for some of those businesses.

With a 20% share of sales and with 26% of food sector employees, meat is the largest food subsector. The French meat industry is composed mainly of small companies, and even French groups are quite small compared to their foreign competitors. According to AGRESTE, following a 1% increase in Q1, meat production decreased 2.0% in Q2 of 2015; mainly due to decreasing prices. Increased pressure on meat prices, especially pork, even led to tense situations and conflicts with producers in Brittany.

Fruit and vegetable prices decreased due to pressure on sales prices, a drop in consumption last summer, and the impact of the Russian embargo. According to AGRESTE, production of processed fruits increased 2.7% in Q2 of 2015 after a 4.1% increase in Q1.

The beverage industry represents 16% of total food sales, and exports about 30% of its sales. Production increased 3.5% in 2014 (excluding wine production). In Q1 and Q2 of 2015 production increased an additional 1.7% and 3.7% respectively, supported by a mild spring. The trade balance remained positive and is still improving, thanks to increasing exports of wine and champagne.

While our underwriting stance towards this sector remains generally relaxed, we are keeping a closer eye on certain subsectors, especially meat and dairy, because of their challenging market conditions. We try to meet our customers' requests whenever possible and, indeed, where our assessment of the buyer or subsector is particularly positive, we encourage the customer to extend credit limits further.

French food sector

Strengths	The world´s fifth largest food exporter
	High reputation for quality food products
	Resilience throughout the economic crisis / non-cyclical industry
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

Germany

- Decreasing sales in 2015
- More insolvencies expected in the long term
- Fraud cases remain an issue

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 decreased 1.7% in 2014, to EUR 172.2 billion. This was followed by another 4.4% decrease in H1 of 2015, reaching EUR 81.9 billion. While domestic sales decreased 6.5%, to EUR 55.8 billion, export sales recorded modest growth of 0.5%, increasing to EUR 26.1 million. Real turnover (domestic and export) declined 2.1%.

Despite decreasing sales, businesses' equity strength remains good in this sector, but larger groups and producing companies are usually better capitalised than wholesalers or retailers. In terms of solvency and liquidity, larger companies are normally better financed than smaller ones. The overwhelming market power of large retailers and discounters and the 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. As a result, their profit margins have decreased in recent years and are continuing to decline. In the last couple of years food discounters in particular have changed their supply practice, reducing the number of suppliers and focusing on a lower number of larger suppliers.

Nevertheless, despite the problems in the industry, many companies in all food subsectors are doing well. The food sector is non-cyclical, and thus less volatile than other industries. Moreover, the sector's export share has almost doubled since the mid-1990s, providing business opportunities abroad. However, while businesses with strong export orientation have tried to increase sales to other export markets after the Russian food import ban, success has been limited so far.

Meat/meat products is by far the largest subsector, controlled mainly by a few market-leading meat processors who, over recent years, have created fully vertically integrated groups. The rising demand for meat worldwide has provided business opportunities for the German meat industry, with a boost to the profit margins of those with the largest export share. However, over-

Germany: Food and beverages sector

	2014	2015f	2016f
GDP growth (%)	1.6	1.7	2.1
Sector value added growth (%)	0.1	-0.5	1.4

Sector share in the national economy (%)	1.5
Average sector growth over the past 3 years (%)	0.0
Average sector growth over the past 5 years (%)	1.5
Degree of export orientation	high
Degree of competition	high

Sources: IHS, Atradius

capacity in the German meat and meat processing sector means that suppliers of non-essential products and those that do not export are in danger of sooner or later being squeezed out of the market.

After positive developments in 2013 and early 2014, thanks to high milk prices and increasing volumes, milk farmers have suffered from substantially decreasing milk prices in 2015. However, the sector benefits from specific EU subsidies.

Due to slightly decreasing market prices, which result from increased available market volumes (also due to the Russian food import ban), turnover is not increasing as much as sales volumes. As a result, profit margins are decreasing.

Despite lower raw material costs for cereals and sugar, sales prices in the German beverage industry (beer, mineral water, soft drinks etc.) remain under pressure because of lower consumption, increasing consumer price sensitivity, overcapacity and discounting. The German beer sector is facing continuing market concentration and consolidation and changing consumer behaviour. The number of breweries still appears too high and many are too small to be competitive. In an attempt to reverse the industry-wide decline in sales of beer, many German breweries have begun to offer innovative beer-mix drinks with lower alcohol level or to produce craft beer, which are and probably will remain niche products without significant market shares. Profit margins continue to shrink in this segment.

Food producers and wholesalers pay, on average, within 30 days while payment terms of food retailers often vary between 45 and even 90 or more days. We have not seen any increase in the number of notified non-payments in the last couple of months and do not expect this in the near future.

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. Still, the already low profit margins are further decreasing. Due to the still strong economic environment in Germany, food insolvencies have not increased recently. However, in the medium term the number of defaults could rise, especially for smaller businesses and those with poor financial strength.

As the food sector´s performance is still robust, our underwriting stance remains generally relaxed, although we can usually provide cover on buyers who have operated for less than a year only if they are affiliated to well-established companies or groups. If there are signs that a buyer's finances are deteriorating, we will increase our monitoring, with quarterly reviews and requests for recent reports of payment experience.

The food sector has seen considerable fraud cases, which are still rising and getting increasingly tricky and professional. 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).

German food sector

Strengths	Non-cyclical industry
	Innovative industry sector reacting on changing consumer behaviour
	Profitable export business
	Internationally very competitive
Weaknesses	Partial overcapacities
	Declining number of consumers and ageing society in Germany
	Shrinking margins
	Low price levels due to strong discount sector

Source: Atradius

The Netherlands

- **Further export growth expected in 2016**
- **Payments take 40 days on average**
- **Some issues in the meat subsector**

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 Netherlands is one of the largest exporters of agricultural and food products in the world. Exports amounted to EUR 80.7 billion in 2014, and the sector accounted for 20% of total Dutch exports (18% in 2013). More than a quarter of food exports consist of re-exports, i.e. foodstuffs that are imported undergo minor processing and are exported again.

Due to the weaker euro exchange rate and increased demand from overseas markets, Dutch food exports increased in 2015, and are expected to rise further in 2016. That said, the Russian import ban still affects the industry, particularly the fruit and vegetables subsector.

In general, demand for Dutch food products is increasing, and profit margins of most businesses are expected to remain stable. Banks are generally willing to provide loans, and businesses´ indebtedness is rather low. The average payment duration is 40 days, and the amount of payment delays, protracted payments and insolvencies is low compared to other Dutch industries. In line with the overall trend in the Netherlands, food business insolvencies have decreased in 2015, and are expected to continue to fall in the coming months.

Supermarket sales grew 1.7% in 2014, an increase almost similar to that of 2013. Again, the increase in revenue was primarily driven by higher volumes (up 1.6%) while prices increased only 0.1%. Turnover of other food, beverage and tobacco stores increased 1.5% in 2014, also driven by volume growth (up 1.3%) while prices were only 0.2% higher. Although the share of online food retail is still small (0.7% , i.e. EUR 320 million), this segment grew 13.5% in 2014 and is expected to grow further in 2015 and 2016.

Competition in the Dutch food service wholesalers sector is fierce. As smaller hotels and caterers are increasingly buying di-

The Netherlands: Food and beverages sector

	2014	2015f	2016f
GDP growth (%)	1.0	2.1	1.7
Sector value added growth (%)	3.4	0.3	1.8

Sector share in the national economy (%)	2.3
Average sector growth over the past 3 years (%)	1.6
Average sector growth over the past 5 years (%)	1.1
Degree of export orientation	high
Degree of competition	high

Sources: IHS, Atradius

rectly from supermarkets because of price advantages, margins remain under pressure in this segment. That said, our general underwriting stance for the retail segment is relaxed.

The dairy sector is an important segment of the Dutch food sector, with 65% of the milk production sold abroad, mainly to France, Belgium and Germany. The Netherlands accounts for 5% of global dairy trade. Since the drop in demand from Russia in August 2014, outside of the EU, China, Nigeria and Saudi Arabia are currently the most important export destinations. Cheese production decreased 2.7% in 2014 as a result of the Russian import ban.

Despite an increase in the processed milk supply in 2014, the lower price levels for dairy products led to a 1.5% drop in the Dutch production value in 2014, to EUR 7.2 billion (down 1.5%). Increased production in several EU member states provided extra supply, which could not be absorbed as demand from China has decreased and the Russian import ban continues. However, since August 2015 the market has revived and prices have recovered. Dairy production is expected to increase 5% in 2015 thanks to the end of EU milk quotas in April 2015.

Our general underwriting stance for the dairy subsector has become more restrictive in 2015 due to lower earnings, but the outlook remains moderately positive, as most businesses in the Dutch dairy processing industry are adequately financed and have a strong market position. That said, buyers who have planned higher investments and are mainly focused on the (currently shrinking) Chinese export market will be more closely monitored.

The current trend of less energy consumption and lower gas prices is especially beneficial for the greenhouse vegetable segment, as lower energy costs help sustain margins. The Russian import ban continued to affect the sector in 2015, as total export volumes decreased 15% in H1 of 2015.

Fruit growers faced an average 20% price decline in 2014 due to a very good crop harvest. They also suffered a considerable income decrease in 2014, and the permanent pressure has forced businesses in the fruit sector to look for alternative markets. The Russian food ban impacted apple exports in 2015, which decreased 14% in H1 of 2015.

Our underwriting stance remains open, as our exposure is mainly focused on businesses at the end of the value chain. Those fruit and vegetable wholesalers mostly record low margins, but show high cost efficiency.

90% of Dutch pork meat production is exported to Europe, with Germany accounting for a 20% share. Pressure on margins is high and expected to remain so in the coming years, due to more quality-sensitive consumers, supermarkets´ bargaining power in price negotiations and overcapacities in the sector itself. We have observed that margins of those businesses with a focus on cost efficiency, innovations and good product quality have stabilised between 5% and 6%, while margins of companies which performed less well decreased to around 1.5%. In general, our underwriting stance for meat businesses remains neutral.

Dutch food sector

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

Source: Atradius

Market performance snapshots

Italy

- **A modest rebound in 2015**
- **Meat sector faces more troubles**
- **Higher insolvency risk for smaller food retailers**

The food sector is one of the most important industries in Italy, which employs around 385,000 people and generated a total turnover of more than EUR 132 billion in 2014. After several years of suffering from the domestic economic downturn, the Italian food sector´s performance was stable in 2014, benefiting from lower raw materials and energy prices. In 2015 a modest production increase of 1.1% and turnover growth of 0.3% is expected, mainly driven by higher exports (up 6%). The sector was able to compensate for losses caused by the Russian import ban with higher exports to the US and the EU.

Profit margins have decreased in 2015, but are expected to remain stable in 2016. Payment delays and insolvencies are also expected to remain stable next year.

So far in 2015 dairy production has grown in absolute value, but not enough to compensate for the general decrease in milk prices, putting pressure on businesses´ margins. Lower demand from China and the Russian import ban have added to that pressure. At least Italian dairy recorded higher export growth to the US, Japan, the UAE or South Korea. However, the outlook for 2016 remains subdued, unless milk prices increase again. The butter and powdered milk segments remain the best performers in this segment.

In the cereals sector prices for raw materials have been generally low, except for wheat prices, which remained volatile after a peak at the end of 2014 and beginning of 2015. In general, higher wheat prices have put pressure on margins in the mill segment. The pasta and bakery segments have benefited from the strong reputation of the "Made in Italy" trademark abroad with increasing exports, while the domestic performance remained flat. The outlook remains positive, with further growth of demand expected in the EU, the US and new market opportunities in Asia.

In Italy, domestic meat consumption has remained below EU average. The beef sector is affected by a change in food habits towards increased white meat consumption. Except for the beef segment, the sector has taken advantage of lower animal feed prices, which led to a small recovery of margins. While it is too early to assess the effects of recent WHO warnings about the negative consequences of processed meat consumption on health, Italian consumers´ first reaction has already been a reduction in meat consumption. We monitor this subsector more closely than others due to its problems, and our underwriting stance is more restrictive.

After decreasing sales in 2014, food retail turnover has increased again in 2015. However, this growth was mainly generated by large scale retailers, while smaller retailers are still recording decreasing sales. Large scale retailers show better capitalisation, stronger market power, a reasonable level of liquidity and access to the bank system, while small- and medium-sized retailers face a higher insolvency risk.

The Italian retail sector remains strongly fragmented, with increasing competition, higher gearing and pressure on margins. Even the biggest Italian businesses are small compared to other international major retail players. It is expected that the concentration process in the Italian retail segment will accelerate further in 2016.

Since October 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. This law was also meant to release further liquidity in the Italian food value chain and help to improve international competitiveness. However, the effects of the law have been limited so far. In many cases additional liquidity has been used to reduce short-term bank facilities, not being substituted with new investments. Additionally, there is still a lack of external monitoring of compliance: many small players are still not complying with Article 62, leading to longer payment terms.

Poland

- Successfully managing Russian food embargo
- Payments take 45 days on average
- New taxes on banks and supermarkets could harm the sector

As in 2014, the Polish food sector has performed well to date. Food producers have benefited from robust domestic demand (which accounts for about 70% of sales) and increasing export. Businesses proved to be able to cope with market environment changes: e.g. in the fruit segment, Polish apple farmers and producers were originally adversely affected by the Russian food embargo. However, apple producers were successful in entering new markets in order to replace discontinued exports to Russia, and even became the world's leading producer of apple juice.

It is expected that in 2015 Polish food exports will reach a historical peak of about EUR 25 billion (EUR 21.3 billion in 2014). The major Polish export destination remains the EU, notably Germany and the UK, but the share of exports going overseas to Asia and Africa is increasing.

The Polish meat subsector continues to grow, although many investments in this segment have been financed externally, as a result of which many companies are highly indebted. Pork production, which accounts for the lion´s share of Polish meat production, is decreasing due to lower pork prices and lower profitability, which has been partially caused by the Russian embargo. However, poultry production has doubled over the last decade, reaching 2.2 million tonnes in 2015, with further growth expected in 2015. Meanwhile, Poland has become one of the major poultry producers in the EU, stimulated by increased domestic demand and higher export sales.

Since the EU milk quota ended in April 2015, the dairy sector has been facing more challenges in the short term. However, in the long term, Polish farmers and dairy producers could benefit from the lifting of production limits, utilizing their full production capacity.

Given its current fragmentation, a further concentration and consolidation process in the Polish food sector is highly probable. With the support of investment funds such a process is already on-going in the food processors segment, while in the food producers segment the process of consolidation is still in its initial phase.

The Law and Justice (PiS) party, which won the October 2015 general elections, has announced the introduction of an extraordinary tax for supermarkets in early 2016. While this was introduced in order to protect smaller domestic-owned retail businesses, it could be a challenge for (mostly foreign-owned) large supermarket chains.

Another issue could be the planned extraordinary tax on banks' assets, as this could have a negative effect on the external financing of Polish businesses – especially in the food sector where dependence on bank finance and overall indebtedness is high.

On average, payments in the food sector still take about 45 days. We expect payment delays and insolvencies to remain stable or even to decrease slightly in the coming months.

As the expected negative consequences of the Russian embargo have largely not materialized, our underwriting stance for the Polish food sector remains quite relaxed. However, we exercise more caution in the retail segment due to the planned tax introduction. The same accounts for slaughter houses and processors in the red meat segment, pork breeding and the dairy segment due to decreasing margins.

Market performance at a glance

Hungary

- The food and beverage industry is one of the most important sectors of the Hungarian economy. It is the second-largest employer and the third-biggest producer in the manufacturing sector, accounting for more than 10% of total industrial output in 2014. Food export revenues are a significant contributor to Hungary´s overall trade surplus.
- In 2014, the food and beverage industry accounted for 7.6% of the total exports, mainly fruit and vegetables, meat products and dairy products, with over 90% of the export destined to countries of the European Union. Over the last five years, the Compound Annual Growth Rate of food exports was 10.7% while domestic sales grew 4.8%.
- While profitability of food producers has increased in 2014 and is expected to remain stable in 2015, one of the main challenges for the industry is the overall high tax burden, that dampens household consumption.
- The average payment duration in the Hungarian food industry amounts to 60 days. The number of protracted payments, non-payments and insolvency cases has remained stable over the last six months, and no increase is expected in the coming months. However, the food sector´s insolvency rate is above average for Hungary (2.7% in 2014). For example, the insolvency rate of food and beverage producers was 3.5% in 2014. Business failures in the food wholesalers segment increased significantly in 2014. Gearing and dependence on bank finance are generally high in the food sector.
- Our underwriting stance remains generally open, as food turnover is expected to increase further and business proftability remains adequate.

Ireland

- The export-driven Irish food sector has recorded increasing demand for its products. Businesses are benefiting from the weaker euro exchange rate, mainly against the British pound sterling, which is a main reason why profit margins have increased and are expected to continue to rise in the coming months, especially in the meat subsector. Domestically, the sector benefits from the rebound of the Irish economy and growing consumer confidence.
- For the Irish dairy subsector the recent abolition of EU milk quotas and sharply decreasing milk prices have led to a short-term decrease in margins and delays in capital expenditure programmes. However, in the long term the lack of quotas is expected to provide new business opportunities for Irish dairy businesses.
- The sector still suffers from the lack of capital expenditure during the years of recession. While banks still don’t provide sufficient loans to the food sector, the situation is improving.
- Payment behaviour in this sector has been very good over the past 12 months. The number of protracted payments, non-payments and insolvency cases is very low, and is expected to remain stable near the current levels in the coming months.
- Due to the generally benign credit risk and good business prospects, our underwriting stance continues to be open for food producers and retailers in general. However, we are a bit more cautious in the fruit and vegetables segment, as there are some businesses with very low margins and exposures exceeding equity.

Russia

- Combined with the economic downturn and Rouble depreciation, Russia´s sanctions on imports of food and agricultural products hit the domestic food sector hard, in particular the fish, meat and dairy subsectors. Prices for food have grown and local production has increased in order to substitute lacking imports.
- Profit margins of many food businesses have deteriorated over the last 12 months, and this negative trend is expected to continue into 2016. In general, Russian food businesses are highly geared and are facing increasing costs for external financing. At the same time, banks are generally willing to provide loans to food retailers, but more restrictive on wholesalers and import-related businesses.
- The average payment duration in the Russian food sector varies between 15 and 40 days, depending on the kind of product. The number of protracted payments, non-payments and insolvency cases has sharply increased over the last six months, especially in the import-related and distribution segments for fish, meat and dairy. While it is expected that insolvencies will not increase further year-on-year in 2016, the number of non-payment cases and business failures will remain on a high level.
- That said, the largest domestic grocery retailers have continued their market expansion and have generally not been affected by the sanctions. Some major Russian agricultural vertically integrated holdings have been growing successfully in the last 18 months, using opportunities that state protection provides and benefitting from the sanctions on EU agricultural imports. The Russian food market is consolidating further, as major national food retail chains are crowding out regional players and wholesalers.
- Our underwriting stance remains restrictive for the meat, dairy and especially the fruit and vegetables subsectors, while being somehow less restrictive on certain businesses in the food retail segment.

Spain

- Spanish food production increased 3.8% in 2014, to EUR 93 billion. Growth was mainly a result of higher exports (up 5.9%), while domestic demand remained subdued. However, domestic demand is expected to improve in 2015, in line with the on-going economic rebound.
- Persistent consumer price deflation in 2014 and 2015 has had a negative impact on businesses’ margins. Profitability ratios have declined due to strong competition and price wars in the food sector, mainly in the retail segment. However, consumer prices have increased slightly in recent months, which could lead to increasing profit margins in the near future.
- The intense price war in the retail segment has left some players in a difficult situation. While the industry is still fragmented, industry consolidation is on-going and companies should gain size and become more competitive domestically and abroad.
- The external financing requirement of food businesses is high, and access to credit (both working capital and long-term facilities) has further improved. Bank lending to food businesses has increased by more than 17% year-on-year in the January-July 2015 period.
- The average payment duration in the Spanish food industry is 70 days. Non-payment notifications have decreased over the past couple of years, and we expect the positive trend to continue, along with the improved outlook: the on-going rebound of the Spanish economy and increasing access to bank loans should result in improved business performance, and subsequently in lower payment defaults and insolvencies.
- The food sector’s resilience and stable payment behaviour makes us supportive in our underwriting stance. However, we are restrictive when underwriting the fruit and vegetables subsector, which, since 2014, has suffered from over-production and a decrease in exports (also triggered by Russia´s import ban). In this segment, insolvency numbers are well above the average of the food sector, and our outlook remains negative, as the trend in payment behaviour continues to be negative and no improvement is expected in the short term.

United Kingdom

- The British food sector is facing decreasing proft margins due to a combination of intensifying price wars in the retail segment, a general decline in volume sales (leading to factory inefficiencies), wage growth and high energy prices. That said, lower commodity prices provide some support to the supply chain, and food importers benefit from the stronger pound against the euro.
- Capital requirement is high in the food sector, as many food companies operate with credit cycles that require high working capital funding. There is a general trend of increased payment terms, causing the credit cycle to increase and leading to additional funding requirements.
- The average payment duration in the UK food industry is 45-60 days. The number of protracted payments, non-payments and insolvency cases has increased in the last six months due to increased pressure on businesses´ margins and larger players squeezing payment terms and prices along the supply chain. Payment delays and insolvencies are expected to increase further in the coming months due to increasing competition for shelf space and adverse contractual terms with retailers. Food business insolvencies are expected to increase by about 15% in 2015.
- Our underwriting stance remains open for businesses in the food sector, but these are subject to close monitoring. We are more relaxed with buyers that currently benefit from lower commodity prices and from the current strong pound Sterling. However, due to volatility, raw material prices and exchange rate developments have to be carefully monitored. For instance, the stronger pound sterling has been beneficial to fruit and vegetables importers, but at the same time contract losses with retailers have negatively affected some businesses in this subsector. As a result of lower lending appetite in the small and medium-sized (SME) segment, we are generally more cautious about smaller food businesses.

USA

- The demand situation for the US food sector remains good, with increasing demand especially in the organic and healthy food segments. Food companies benefit from lower raw material/packaging and transportation costs, although some of these benefits have to be largely passed on to the consumer in more competitive segments. Distributors, in particular, are seeing pressure eased a bit against their already tight margins. Overall, profit margins of food businesses are expected to remain stable in 2016. In the retail and food service sectors, competition is very high and companies are prone to undercutting others' prices to gain market share.
- Many food companies, particularly distributors, are very highly leveraged but supported by capital markets given positive cash flow. However, the cost of financing rises as leverage increases. There are many mergers and acquisitions in the food industry, with banks mostly willing to provide financial support due to the benign economic environment. Private equity companies are investing heavily in the food market.
- The average payment duration in the US food industry is 15-60 days, depending on the items sold (e.g. perishable goods or packaged goods). The number of non-payments and insolvency cases has remained stable over the last six months, and no increase is expected in the coming months. Given the recent high level of mergers and acquisitions, companies are being bought and sold - which should result in fewer insolvencies and further efficiencies due to increased synergies.
- As a result of the generally satisfying credit risk and good business prospects, our underwriting stance continues to be open for food producers and retailers in general. However, in light of a recent Avian Flu epidemic in the US, we are more cautious when reviewing single meat companies that could be affected. In the dairy subsector we more closely monitor export-dependent businesses, as exports have weakened while domestic demand remains strong.

Industries performance forecast per country

December 2015

	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	N/A	☁	☁	☁	⛅	⛅	⛅
India	☁	☁	⛅	🌧	☁	☁	☁
Indonesia	⛅	🌧	☁	☁	☁	☁	☁
Japan	⛅	☁	☁	☁	☁	⛅	⛅
New Zealand	⛅	🌧	⛅	⛅	🌧	⛅	⛅
Singapore	⛅	🌧	☁	🌧	☁	☁	⛅
Taiwan	N/A	🌧	☁	☁	⛅	⛅	☁
Thailand	☁	☁	☁	☁	🌧	☁	☁
United Arab Emirates	☀	⛅	⛅	☁	☁	☁	⛅

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

Excellent
Good
Fair
Poor
Bleak

Industry performance

Changes since October 2015

Europe

France

Consumer Durables

Up from Poor to Fair

The business climate in the retail sector has improved and French households´ purchasing power has increased. Credit insurance claims have decreased.

Services

Up from Poor to Fair

The business climate in the service sector has improved and credit insurance claims have decreased.

Italy

Consumer durables

Up from Fair to Good

Positive expectations for the sector's performance in Q4 of 2015 due to improving consumer confidence and a modest economic rebound in Italy. The credit insurance claims situation remains stable.

Services

Up from Fair to Good

The growth outlook remains stable and results in specific sub-sectors like tourism have improved. The credit insurance claims situation remains stable.

Transport

Up from Poor to Fair

The sector has shown signs of rebounding in 2015 due to lower fuel prices and lower interest rates on leasing contracts. Transport is expected to benefit from the on-going economic recovery.

Poland

Agriculture

Up from Fair to Good

Polish farmers have successfully overcome difficulties in connection with the Russian food import ban.

Portugal

Chemicals/Pharmaceuticals

Down from Fair to Poor

In 2015 payment behaviour has deteriorated in several subsectors.

Spain

Construction

Up from Bleak to Poor

After years of severe contraction, the industry finally shows the first signs of a rebound due to the on-going economic recovery, foreign investments and the return of business confidence. Infrastructure construction is expected to grow due to government investment in rail and road infrastructure.

Sweden

Consumer Durables

Up from Fair to Good

Electronics/ICT

Up from Fair to Good

Both sectors have recorded decreasing insolvency figures, and the outlook remains benign.

The Americas

Mexico

Electronics/ICT

Down from Fair to Poor

Both decreasing commodity prices and a volatile exchange rate have a negative effect on the performance of large mining businesses, which have to reduce costs and cancel projects.

Asia/Oceania

China

Metals

Down from Poor to Bleak

The sector suffers from sharply decreased commodity prices, the current domestic economic slowdown and overcapacities.

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