

Fast Facts on Food Processing

Grant Thornton Food & Beverage Practice Part 3 of 6

Growth, Projections and Reflections

Arguably, 2008 has been the most challenging year in decades for most industries. With the current economic recession making consumers fearful of overspending, food and beverage manufacturers have anxiously looked out over their markets — groceries and other retail outlets, eating establishments, etc. — trying to project their sales opportunities (or lack thereof). Most food and beverage manufacturers, though, remain reasonably optimistic about this year and next.

Grant Thornton LLP, the audit, tax and business advisory firm, is collaborating with *Food Processing* magazine on a series of six bimonthly surveys — *Fast Facts on Food Processing* — to provide a current picture of business performance challenges and opportunities in the food industry.

This third survey — *Growth, Projections and Reflections* — examines how food and beverage manufacturers fared this year, the factors affecting their companies, and how they expect to perform in 2009. Responses were received from 105 companies (see participant profile at the end of this report) in October and November 2008.

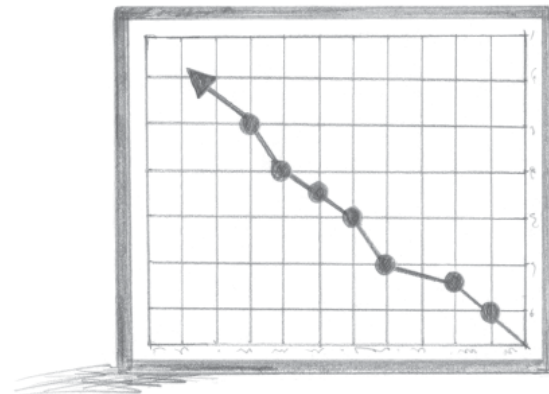
Revenues and profit growth

A majority of food and beverage manufacturers (64%) indicate that revenues will increase in 2008 vs. 2007. Twelve percent report that revenues should hold steady. Even amid the current recession, which most economists project will last at least through the first-quarter of 2009, 72% of food and beverage manufacturers anticipate that their revenues will increase in 2009 vs. 2008, while 12% expect revenues to remain steady. Few food and beverage manufacturers expect steep revenue declines in either 2008 (9% expect revenue declines of more than 10%) or 2009 (6% expect revenue declines of more than 10%).

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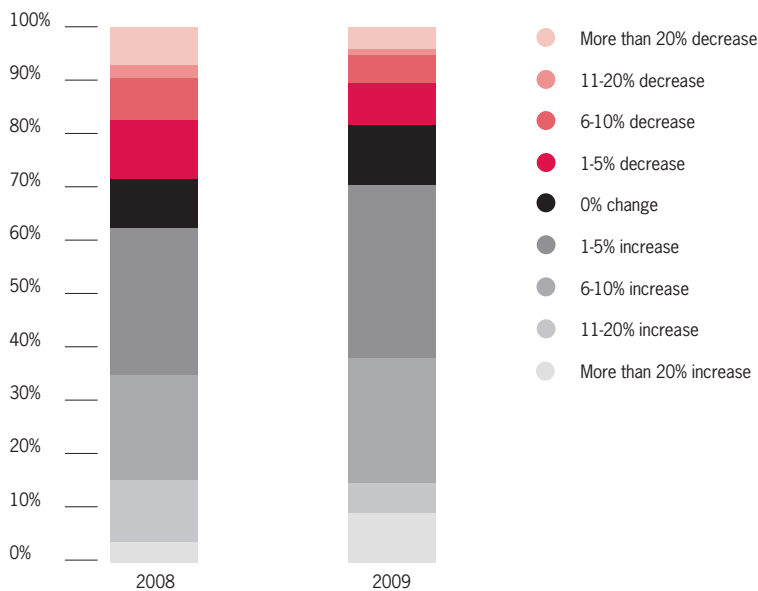


Most food and beverage manufacturers are turning this top-line growth into bottom-line growth as well. A majority (63%) report that profits will increase in 2008 vs. 2007; 9% expect profits to remain steady. Looking to 2009, 70% expect profits to increase vs. 2008; 13% of firms anticipate that profits will be unchanged. Similar to revenue projections, few firms expect steep profit declines in 2008 or 2009 (see Profit Growth chart).

Food and beverage executives report that they used a variety of strategic and/or operational techniques to help their companies grow in 2008, including:

- **Inventory management** — reducing inventory they are holding as well as regional consolidation of inventories
- **Cost controls** — eliminating overtime, renegotiating shipping and storage contracts, reducing and refocusing advertising and marketing expenditures by product line, and shedding non-core businesses
- **Sales efforts** — increasing distributed sales to counter decreases in custom manufacturing, contacting different store markets (e.g., convenience stores), expanding the customer base to avoid reliance on too few customers, expanding a private-label program, and increasing prices
- **Acquisitions** — “...bought existing plants from other firms exiting segments that our company is gaining market share in.”
- **Innovation** — launching new products, diversifying product offerings, and “...expanding the types of manufacturing services we are able to provide our clients.”
- **Process improvements** — “...continuous process improvements led to small but important improvements in margins that helped maintain revenue and profit levels,” consolidation of manufacturing, improving site utilization, outsourcing IT and other non-core functions (e.g., facility maintenance, testing), and reviewing and restructuring administrative positions

Profit growth % of food and beverage manufacturers



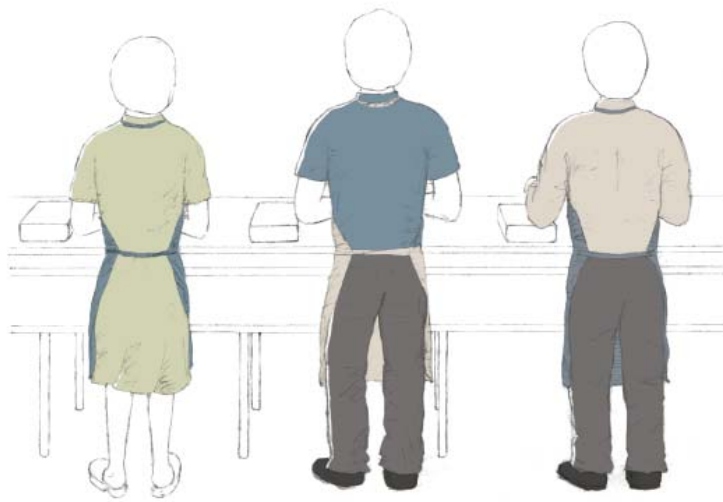
One executive noted that a poor economy has meant good business: “The downturn in the economy caused increased product purchases by consumers of the products that we sell.” But another executive notes, “At this time we are in a slow growth pattern, yet are hopeful that the economy will improve.”

The economy is on the minds of many executives, and it appears to be nipping at some margins. Profitability was most adversely affected in 2008 by fuel/energy costs (80% of food and beverage manufacturers), ingredient material costs (68%), the state of the economy (52%) and health insurance costs (32%). In 2009, the factors most likely to negatively affect profitability are the state of the economy (67%), ingredient and material costs (60%), fuel/energy costs (55%) and health insurance premiums (35%).¹

¹ For these questions, respondents were allowed to select more than one answer.

Staffing levels

Despite optimism for revenue and profit projections, food and beverage manufacturers are taking a cautious approach to managing the size of their workforce. Approximately one-third of firms (34%) will make no change to the number of full-time employees and equivalents for 2008 vs. 2007; 38% of firms plan to increase workforce sizes, but most of that increase is in the 1-5% range (25% of firms). Projections for 2009 are nearly identical, with 37% indicating no change and 37% expecting to increase workforce sizes (24% of firms will increase by 1-5%).



Looking ahead

If the second half of 2008 taught business executives anything, it's that it is difficult to know what really lies ahead. That point is evident in comments from food and beverage executives when asked about their prospects for success in the coming 12 months.

Many executives look outside their companies and see reasons to be optimistic. For example, one executive sees stability coming from recent efforts to shore up the banking sector: "I am optimistic that things will get better in the next 12 months. With the bailouts giving the economy a boost, we may be able to see light at the end of the tunnel, even though the next six to eight months will be rough."

But there also is considerable pessimism among food and beverage executives regarding the business conditions around them. "Raw material costs will increase significantly due to the influence of 2008 commodity prices on 2009 ingredient costs," says one executive. The same executive also notes, "higher retail prices for our products will have a negative effect on total sales."

Another says that suppliers have raised raw material prices nine times in 11 months. Others cite concerns about expanding government influence under a new administration, a strengthening U.S. dollar reducing exports and the proliferation of overseas sourcing. "U.S. companies are willing to gamble against major recalls or class-action lawsuits by contracting with Asian companies for finished products. We cannot compete against their overhead costs (energy, healthcare, wages, etc.) even with a superior product."

One executive goes even further: "This whole country is in bad shape. We've lost what made America great, and it would be hard if not impossible to recover. Welcome to the world's dumping ground — the USA."

Yet even as many comments focus on the economy and its ramifications, business success still ultimately rests on the actions these companies have taken. For example, one executive reports, "Our market share is declining in a sector that is shrinking. Our QSR (quick service restaurants) competition has out-innovated us in our own backyard."

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Still, many executives believe they have put their companies in a position to succeed:

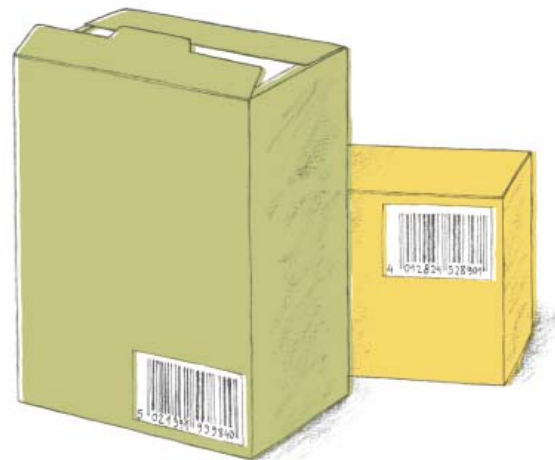
- “Projects that were initiated this year and in prior years will be coming to fruition in the coming 12 months.”
- “I believe the company is well positioned to meet consumer demand for a product that shows no sign of slowing. The only uncertainty is to what degree the global economy will impact this demand.”
- “We are extremely optimistic for 2009 as we have been aggressively updating our QA/HACCP (quality assurance/hazard analysis and critical control point) plans, redefining the focus of our business, directly managing our growth by using consultants and other resources, and are bringing on several new customers. In short, we are dedicated to making this business successful and have taken the control we lost over the last several years back into our own hands.”

How is your firm managing? Which initiatives and strategies are working for your company’s success? Which aren’t and what are you doing about it? •

Profile of Participants

A diverse group of food and beverage manufacturers are represented in the results of the third survey. One-quarter of survey participants (25%) report annual revenues greater than \$500 million, and 25% report revenues of less than \$5 million. Approximately 39% of companies produce processed foods, the largest food group represented, followed by miscellaneous/other (35%); meat, poultry and seafood (32%); and beverages (31%).*

* Participants were able to select more than one answer category.



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About Food Processing

Established in 1940, Food Processing is the premier publication for the packaged foods industry. Food Processing writes for the entire management team about the critical issues in bringing a product successfully to market, exploring the latest trends in new product development, marketing, process optimization, packaging and workforce management.