

## Summary of hearing with Northern Ireland Food & Drink Association

### Background

1. The Northern Ireland Food & Drink Association (NIFDA) represent approximately 120 food, drink and animal feed manufacturers (out of a total of 230) in Northern Ireland. NIFDA do not have any formal relationships with the various retail organizations in Northern Ireland, but routinely meet them throughout the year. NIFDA have two trade association members: the Northern Ireland Meat Exporters Association and the Northern Ireland Grain Trade Association. NIFDA is a member of the Confederation of British Industry Northern Ireland and the Trade Association Forum, and, is affiliated to the Food and Drink Federation UK.
2. Food and drink manufacturing is an extremely significant sector of the Northern Irish economy. NIFDA's members account for about 80 per cent of the (£2.5 billion) turnover of the food and drink manufacturing sector in Northern Ireland and about 67 per cent of that sector's employment. The agri-food industry represents a significant share (about 7 per cent) of Northern Ireland's GDP. About 60 per cent of the products are exported, mainly to Great Britain and the Republic of Ireland. Most of its members supply the grocery market and the catering trade.

### The market

3. The turnover in the manufacturing sector increased from £2.215 million in 1995, (before the multiples entered the Northern Irish market) to £2.507 million in 2004. The profitability of the manufacturing sector, however, declined during the same period (from 3 to 2.9 per cent) while the profits of grocery retailers (both the multiples and independents) had increased. The total value added as a percentage of sales increased from 16 to 19.2 per cent. The arrival of three multiples in 1996 had a noticeable effect on the Northern Irish Market in that 60% of the market changed hands. The independents had recently started to follow a similar path to the multiples with many combining into larger groups. There were virtually no stand-alone independents remaining, because many had become part of a 'buying group'. In turn, these buying groups had also started to combine. This trend meant that manufacturers had a reduced choice of groups or chains through which they could sell to consumers.
4. The reduced profitability and poor return on working capital, along with a volatile market and contractual issues had created difficulties within the industry with regard to investing for the future. NIFDA members had not made specific complaints about these issues because of the potential for reprisals: smaller members believed their grievances could be traced.
5. Weekly price benchmarking prevented any significant price differences between the major grocery retailers which benefited consumers as prices remained relatively steady. This meant manufacturers and exporters did not have the option of increasing prices when manufacturing costs rose, because a grocery retailer could not allow its prices to differ from its competitors and would only increase prices in unison. NIFDA also noted the expectation of exclusivity by grocery retailers (relating to the supply of own label). In addition, Northern Irish manufacturers had to deal with a number of costs outside their control: raw material prices; the highest electricity

costs in the UK; effluent charges; and industrial de-rating, a feature peculiar to Northern Ireland.

6. NIFDA explained how market variables favouring consumers in this way had a profoundly negative impact on regional produce. Regional products had a higher cost base than national products, partly because they were produced in smaller volumes and had to compete with national pricing. NIFDA emphasized that while differences between the economics of regional food production and national food production was a global issue, the problem had been magnified in Northern Ireland due to the paucity of its market (1.7 million) and its dependence on agri-food in its economy.

## **The supply chain**

7. NIFDA said that the number of outlets in Northern Ireland had decreased but had become larger in size. The iconic and truly independent small shops had disappeared from the market. NIFDA explained that while the independent retail sector in Northern Ireland was strong, figures had been based on forecourt retailing statistics and therefore included petrol.
8. The consumer had less local choice now than ten years ago, because the increase in the sector's size was the result of an increase in the Stock Keeping Unit (SKU) count (the number of any one specific product available for sale), not an increase in product variation. Evidence indicated a deflation in food prices and NIFDA believed this reflected that lower production costs were the most important of the market dynamics. NIFDA thought this would eventually lead to a reduction in food production in Western Europe because global sourcing would target countries where food production costs were lowest (generally outside of Europe). NIFDA believed global sourcing would increase unless market forces such as climate change, carbon dioxide, food miles, regional food and consumer choice became predominant.
9. The size of the multiples stores had increased but the area within them allocated for food items had decreased. The emphasis in store capacity had shifted to more profitable non-food items. This included items such as clothing, books, mobile phones, banking services, etc. Priority was given to a primary item, a middle item, and then a value item. The regional product generally had the lowest priority and was often the first to be eliminated. NIFDA members were mostly engaged in regional product so usually suffered greatly from this strategy.
10. NIFDA told us of the closure of two member companies within the past ten years: a poultry processor and a bakery. Several smaller organizations had also amalgamated. Different levels of profitability and conflicting opinions regarding industry problems were evident from the various sectors of NIFDA's membership. NIFDA had been unable to comment on specifics due to the potential exposure of these companies.
11. There had been relatively limited merger activity by larger member companies, despite the strong commercial pressures to consolidate. Many independents had been family-owned for generations so were more resistant to acquisitive behaviour. NIFDA stressed the difficulty in concluding simple patterns of merger activity because other members were global multinationals and were naturally acquisitive. The financial logic of combining to reduce costs meant that greater merger activity could become likely in future.
12. Most of NIFDA's members were small and medium enterprises and worked with extremely limited information when compared with the multiples, which had access to a global network of data. This data included, for example, information relating to

market trends, pricing developments and alternative sources of supply. Smaller members had to absorb the costs of trends or unforeseen events that multiples could predict or prepare for. The multiples had benefited from shelf ready packaging that NIFDA members were paying for, this initiative increased NIFDA member labour, packaging costs, packaging waste and reduced multiple labour.

13. The most pressing issue for NIFDA's members had been the lack of transparency in contracts. The processes involving ombudsmen or arbitrators had rarely been used because of the fear of reprisals. If terms and conditions were clearly documented and contracts more transparent, arbitrators would be able to pass judgments with less difficulty during disputes. Such a change would reduce instances of bad practice or retrospective contract adjustments.

## **Regional produce**

14. Some suppliers had benefited from the entry of the multiples into the Northern Irish market because supplying the multiples ensured national sales. The downside of that had been that smaller manufacturers which supplied specialty, niche or regional products (and did not supply to the national market) found it more difficult to compete. This imbalance had concentrated the market at the grocery retailers' end of the supply chain. This was reflected in statistics that showed no growth other than inflationary in the sector's turnover. NIFDA expressed concern about this trend, and feared that regional products would eventually be streamed out.
15. NIFDA spoke of its involvement in the 'Taste of Ulster' initiative, in which it had engaged with its members to promote local foods. The government had also launched a 'Food Strategy Implementation Partnership' programme, which budgeted £4.5 million to inform consumers about regional products.
16. NIFDA told us of the disagreement surrounding branding standards and the debate over what constituted a 'local' product. A technical definition applied by NIFDA stated that at least three-quarters of the value added must have occurred in Northern Ireland. This included products, such as orange juice, that had not been manufactured from locally grown material but had been formulated to local tastes. The farm-based view was that local products should have been manufactured and produced within the region from start to finish to qualify as 'local'.
17. NIFDA was concerned that the multiples might ultimately stream out regional produce thereby reducing consumer choice and raising quality issues. In one particular example, a multiple only agreed to sell a new regional product from a member provided the cost to them was half the proposed price. NIFDA advised the member not to supply. NIFDA illustrated how value lines had set a benchmark price in the consumer's mind by keeping overall prices as low as possible. This made getting a return on new research and development led products very difficult and stifled consumer choice.
18. Regional products were still popular but were not profitable. Issues that negatively affected their market share included: lack of return on capital employed; lack of profitability; market deflation; national pricing; and global sourcing. Multiples had only recently attempted to remedy the problems affecting regional produce. NIFDA highlighted the national pricing policy, where a product's price was the same throughout the UK regardless of different cost bases and regions, as the biggest obstacle for the smaller members. A uniform retail price structure had seemed logical from the perspective of the multiples but had also been demanded of the manufacturers.

19. NIFDAs members had not charged independent retailers higher prices despite the fact that the prices its members received from the grocery retailers had been restricted by the multiples' bargaining power. The supermarket multiples benefited from volume discounts rather than a basic price differential.
20. The strategy of factory gate pricing often left manufacturers having to spread higher distribution costs to smaller independent customers. This therefore acted against product accessibility and pricing for consumers.

### **The Supermarket Code of Practice and planning issues**

21. The Supermarket Code of Practice (SCOP) had not changed anything although the dynamics of the marketplace had begun to change. NIFDA believed the SCOP should be enforced by an independent ombudsman.