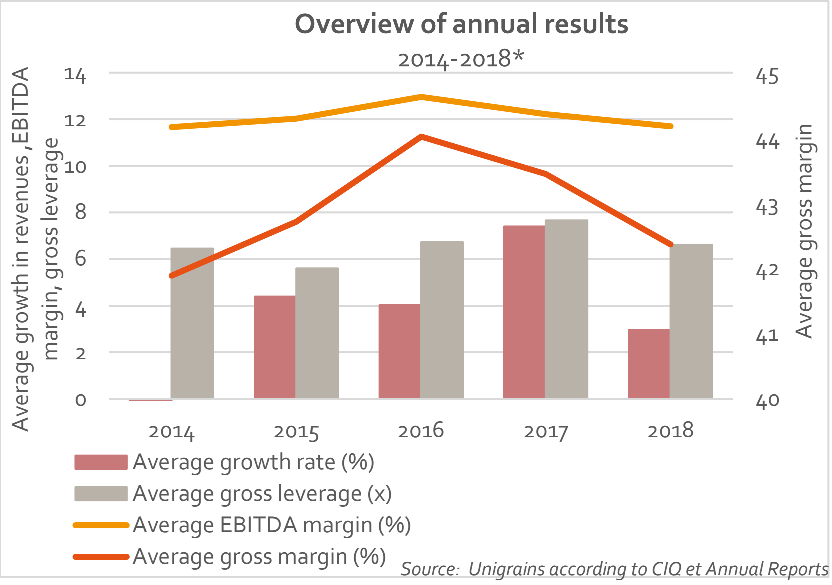
Unigrains – In Brief

French agri-food industry: how to deal with pressure from food retailers?

Unigrains reviews the options through the listed companies' the annual results



Companies included	Sector
Advini	Wine & Spirits
Bel	Dairy
Bonduelle	Fruit & Vegetable
Danone	Sweet & Savoury Groceries
Eurogerm	Food Ingredients
Fleury Michon	Meat
Lanson-BCC	Wine & Spirits
Laurent-Perrier	Wine & Spirits
LDC	Meat
Marie Brizard	Wine & Spirits
Pernod Ricard	Wine & Spirits
Poulaillon	Sweet & Savoury Groceries
Remy Cointreau	Wine & Spirits
Sabeton	Sweet & Savoury Groceries
Sapmer	Seafood
Savencia	Dairy
Tipiak	Sweet & Savoury Groceries
Vilmorin & Cie	Seeds
Vranken-Pommery	Wine & Spirits

* The fiscal year of some companies included in the chart don't end on 31 December: 30/06/2018: Pernod Ricard, Vilmorin & Cie; 30/09/2018: Bonduelle, Poulaillon; 28/02/2019: LDC; 31/03/2019: Laurent-Perrier, Remy Cointreau

Declining sales growth rate and operating margins: the food retail factor isn't negligible

The average sales growth rate of the listed agri-food French companies (renamed "FRAGRO" in the rest of the document) slowed down in 2018. The 2017 decrease in average gross margin continued and even accelerated in 2018, down to 42.4% from 43.5%. This deterioration had a knock-on effect on the average EBITDA margin, which declined from 12.5% down to 12.2%. One of the drivers, although obviously not the only one, is the strong exposure of a significant part (11 out of 19) of these companies to the French food retail industry. Several of them reported difficulties to fully pass their cost (raw materials, salaries, energy etc) increases on to their retail customers, which also struggle to maintain their own profitability in a context of atone consumption and intense competitive pressure.

Rebalancing marketing power and et reducing the dependency on food retail: the strategic options

Through the review of the FRAGRO companies' annual results, Unigrains could draw an extensive overview of the various strategic options adopted to face margin compression, or even a decrease in sales driven by their exposure to food retail. Unigrains distinguishes the measures which aim to reinforce the marketing power of these groups, from the measures they take to diminish their dependency on this distribution channel.

- *Rebalancing marketing power:*

Amongst the FRAGRO companies the commonly applied strategic measure consists in premiumising their product offering. This enables them to better follow the change in consumption habits, in order to maintain volumes and be less exposed to price sensitive customers. For instance, Poulaillon focuses its food retail sales on premium and bio sandwiches, while Fleury Michon put in place an « eat better » strategy with more qualitative products. Bel is

Auteur : Anne COUDERC – tél. : 01 44 31 16 27 – acouderc@unigrains.fr – **Date de Publication :** juillet 2019

changing its offer from melted cheese portions towards "healthy snacking", thus creating a larger and trendier portfolio of products.

This move is often completed by a reinforcement of the innovation effort, whether with or without a broadening of the product offering. Sabeton and Tipiak reported they had increased the frequency of new product launches in an attempt to gain market shares. This should underpin an improvement in their market power towards their food retail clients. LDC accompanies the changes in consumer habits by innovating, notably in the plant-based and organic segments. Bonduelle has extended its activities to the fresh-cut, ready-to-eat vegetables, as this segment is currently experiencing a strong growth. Fleury Michon has enlarged its product portfolio by acquiring Paso Traiteur, a specialist in deli foods.

Some other companies are changing their portfolio mix towards a higher share of branded products, which are often more profitable than private labels. This is the case for Advini, Sabeton and Tipiak.

- *Diminishing the dependency:*

In order to reduce their exposure to the French food retail industry, many companies develop their sales in other distribution channels. For example, the external growth deals completed by LDC in 2018 enabled the group to diversify its distribution circuits towards industrial and foodservice customers, for which growth prospects are rosier. In 2017, Sabeton launched a new brand dedicated to the organic specialised retail store networks. It also focuses its commercial efforts on the food service channel. Both segments' sales grow faster than the food retail ones.

Exports can be another interesting way of diversification. Although its sales are still marginal in these countries, Sabeton directs its commercial efforts on Germany and China. Similarly, Tipiak seeks to accelerate its export sales and has increased its investments to support their development. In 2018 the group's branded products revenue growth of 3.3% was fully driven by its export activity, which jumped by 49%.

Last, some companies chose to settle outside of France, in less mature markets. The acquisition of Ready Pac Foods, an American leader in single-serve salad bowls, significantly increased the size of Bonduelle's activities in North America. Their weight now equals the EU's. On its side, Savencia clearly showed its intent to diversify outside of France by acquiring 3 groups in a row in 2018: one in the US, one in Russia and one in South Korea.

Cost saving plans as an additional support:

Even though their commercial relationships are often difficult, the food retail industry remains and will remain a key client for the French agri-food industry. In order to offset the pressure it exerts on their margins and remain competitive, they implement cost saving programmes. As soon as 2017 Fleury Michon put in place a competitive plan aiming to "reorganise the Group in order to work in a faster, more efficient and thriftier way". The company also ceased its Norwegian business, which was not profitable enough. In March, Savencia announced the closure of three European plants. In order to make savings, it also chose to mutualise the transversal functions (administrative, commercial etc) between the remaining plants. Similarly, in September 2018 Bel announced a vast reorganisation and cost saving programme, which includes a staff reduction plan.

Effects of these strategies: the reality check

Only a few FRAGRO groups provide the financial markets with a precise 2019 guidance. Some companies such as LDC, Sabeton or Danone can already feel some positive impacts from their strategic measures, but these generally take time to bear fruit, and the food retail environment remains difficult.

Nonetheless, the improvement in consumer confidence, if confirmed, could support a shinier short-term horizon. At 101 in June, the consumer confidence index provided by the INSEE grew for the sixth consecutive month and beyond the long-term average of 100 for the first time since April 2018. In addition, the full effect of the newly implemented Egalim law will be assessed at year end. In the press release announcing its results for the financial year ending 31 March 2019, Sabeton mentions that following the law application and the decrease in promotional pressure on the national brands, its private label sales came back to growth.