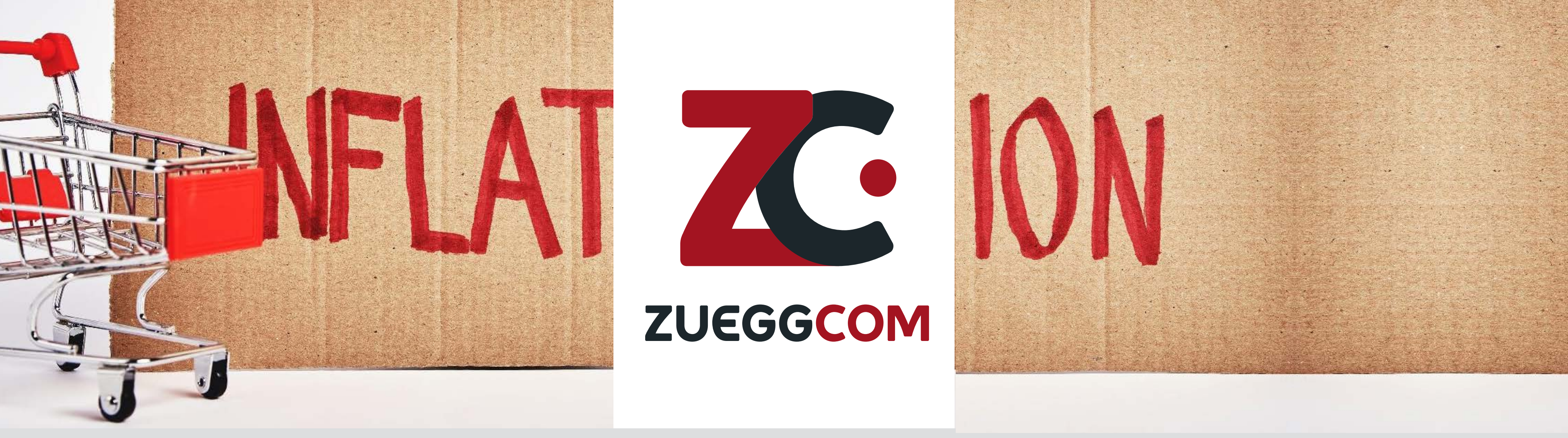

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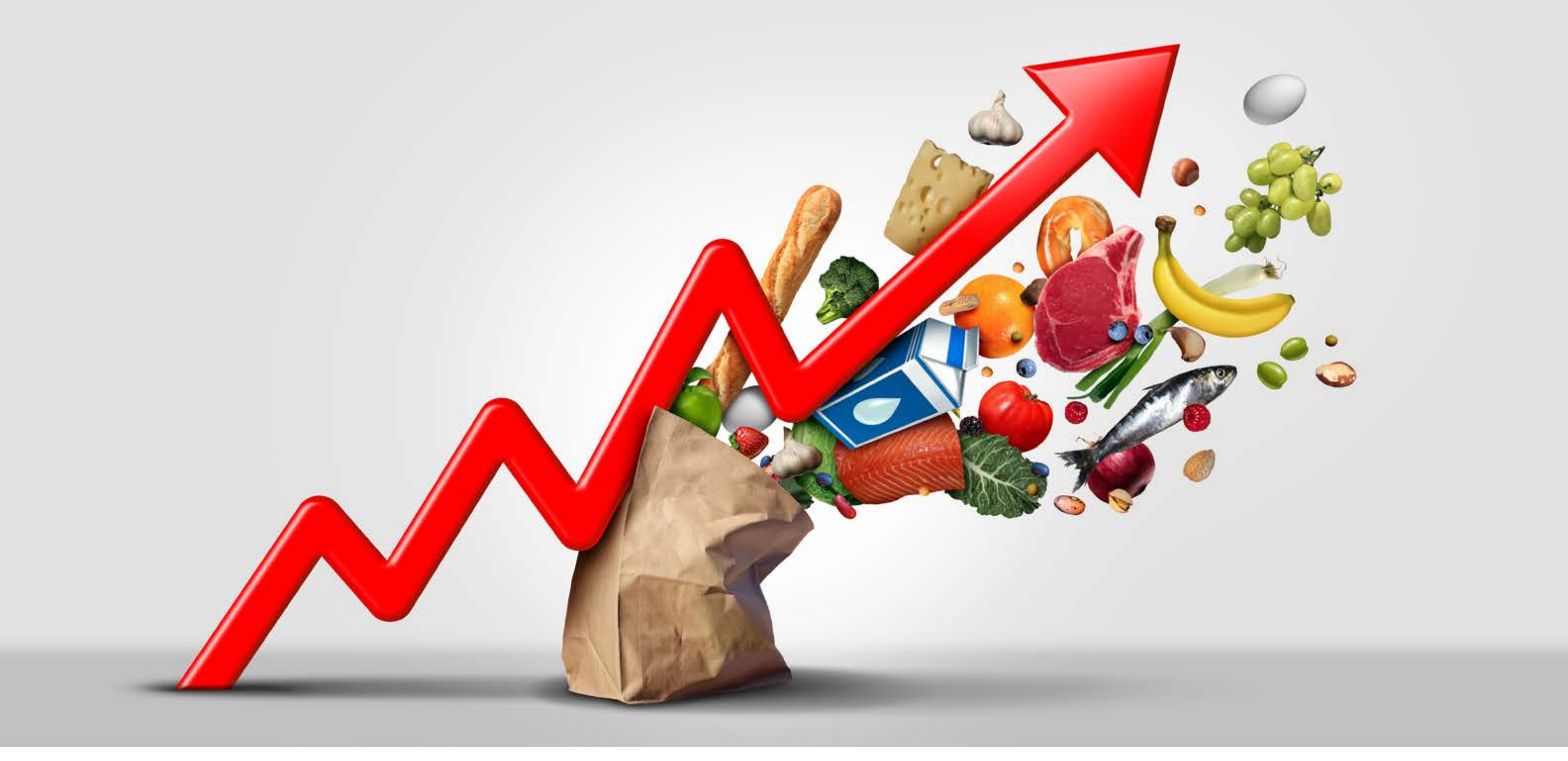
IMPACT OF INFLATION ON F&B INDUSTRY IN THE EUROPEAN UNION

The global inflation rate has risen more than twofold in the last six months. European nations are especially affected, with the European Union (EU) reporting inflation rate of 14% for food and non-alcoholic beverages in August 2022. The overall inflation rate for the region was an extremely high 10,1%.# For instance, Germany reported annual inflation of 10% in September 2022, a new high since the 1990s reunification. The UK recorded the highest inflation rate in the last three decades — 5,5% on the CPIH index and 6,2% on the CPI index. Italy also posted the highest inflation rate in 37 years (8,9%) in September 2022.*

THE IMPACT OF THE RUSSIA—UKRAINE WAR WAS GLOBAL AND THE EU WAS AT THE RECEIVING END:

- The war made it impossible for Ukraine — the "breadbasket of the world" — to send across grains, leading to global food inflation. About 25 million tonnes of wheat needs to be replaced to meet the global demand.
- Russia and Ukraine are the major suppliers of sunflower oil and corn. Together, they cater to 65% of the global demand for sunflower oil. The war also halted the export of these commodities, thus creating a huge shortfall*.
- The price and inputs required for agri-food production, which were already at record levels, further increased.
- The approach of some countries to these challenges is to exert control over the export of essential agricultural commodities, which could amplify the issue of food shortage.

About 400 million people across the globe rely on Ukrainian food supplies. As per UN Food and Agriculture Organization (FAO), "around 181 million people across 41 countries could face a food crisis or worse levels of hunger this year" due to the war.##



IMPACT ON FOOD MANUFACTURERS

As recession looms and inflation rises, F&B owners are forced to choose between developing other capabilities or liquidating their business. M&A deals are being signed to rescue brands. Two major sales were recorded in 2022 — Founded by Swiss winemaker Bernard Fontannaz, Origin Wine saved the millennial-targeted HUN Wine based in London. In supermarkets, UK-based Morrisons bought McColl's 1100 stores. Moreover, manufacturers and suppliers are in conflict as supermarkets pressurise suppliers to absorb price hikes. Recently, Heinz stopped supplying to UK retailer Tesco because the retailer indicated it would not pass on unjustified increase in pricing.

IMPACT ANTICIPATED ON EU FOOD SECURITY

Food availability in the EU is currently not under threat. The block is largely self-sufficient in terms of essential agricultural products and most animal products. Nonetheless, the EU is a significant net importer of certain products that may be difficult to replace quickly, such as seafood and sunflower oil. Furthermore, the crisis revealed the reliance of agricultural production in the EU on several important imported inputs such as energy, animal feed and feed additives, and agricultural fertilizers. As fertilizers account for 18% of the agricultural input costs, trade distortions may be especially severe.

The cutdown on fertilizer production due to record high gas prices has led to scarcity of CO2 (an important by-product) which is affecting the production of soft drinks and beer. Many companies, such as mineral water company Sanpellegrino in Italy, reduced production due to CO2 shortage. In England, the beverage industry requested the government for a contingency plan to keep CO2 flowing.

In addition, the affordability of food for low-income households, which have been impacted by the pandemic, will diminish. In 2020, 8,6% of the EU's total population could not afford a meal of meat, fish, or a vegetarian equivalent every other day. This will worsen the situation.

CONSUMPTION TRENDS

The F&B trends in Europe are being shaped by the recession and geopolitical tension.

- European households will continue to struggle with high food prices. Food and beverage manufacturers in the Eurozone hiked their prices by 14% on average in 2021, with daily items such as oil and fat (+53%), flour (+28%) and pasta (+19%) recording the most increase. In UK, the cost of staples such as pasta and tinned tomatoes rose to 8.6% from 7.8% in September 2022. Prior instances of excessive food inflation demonstrate that retail prices react to producer costs. Significant inflation and reduction in food volume sales in stores will strain the profitability of European food merchants with generally high pass-throughs to consumer prices.
- Severe disruption led to shortage of cooking oils (sunflower oil, in particular) and contributed to the increase in the prices of substitutes (olive oil). The scale and breadth of increase in other categories indicate pricing concerns began long before the conflict, reflecting a broad rise in production costs.
- As food products are necessities, total consumption in volume terms is more resistant to economic downturns than consumption of non-essential goods. In the Eurozone, household spending on food as a percentage of absolute value has never been negative and only slightly negative in terms of volume in 2008, 2012 and 2013.**

CONCLUSION

Over the last seven decades, there have been four significant global economic downturns: in 1975, 1982, 1991 and 2009. While the IMF suggests recessions typically endure one year in developed nations, according to the National Bureau of Economic Research (NBER), a global recession usually lasts 11 months. However, outliers such as the ongoing war between Russia and Ukraine may extend this period. Furthermore, the global economic situation is influenced by growing financial speculation in various sectors, which is bound to influence its recovery.

For F&B companies this means that a combination of inflation and recession will simultaneously drive up costs and severely dent consumer spending. Companies who can quickly react to these challenges by providing consumers with innovative affordable solutions will emerge victorious.

That said, the global economy could show signs of recovery by the end of 2023, in which case the F&B trends will start turning positive. In the meantime, however, reading the market correctly and reacting accordingly will be key for the F&B industry.

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