State of Industry Report
Q2 2024

food & drink federation

Executive summary

- Business confidence fell to -6% in Q2, the first negative result since Q2 2023. A sharp drop in SMEs' confidence was the main driver of the overall fall in confidence.
- 70% of manufacturers are primarily focused on growing UK sales, with new product development ranked as the second highest growth strategy.
- About half of the respondents are planning to keep their investment expenditure on R&D, skills and training, and buildings unchanged, while over half (56%) are planning to increase their investments in plant and machinery.
- Uncertainty about demand and changes to the business environment (50%) and uncertainty about upcoming regulation (47%) will continue to limit investment.
- Key policy priorities for industry with the new government are the UK's relationship with the EU (50%), employment and skills policies (39%) and packaging reforms (36%).
- Industry's labour shortages stood at 4.9% compared to 5.0% in Q1, and remained above rates in wider manufacturing (2.6%) and the UK (2.8%). Skills shortages continue to impact different roles and levels, from engineers and managers to factory operatives.
- 58% of manufacturers would like funding prioritised for novel and alternative packaging, and 55% for resource footprint measurement and reduction.
- 62% of respondents would like to use Apprenticeship Levy funds for first line manager development, and 56% for both business improvement techniques and engineering conversion modules to upskill.

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Read more from **FDF business insights and economics**

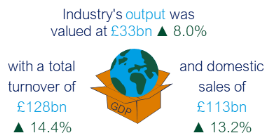
Prices dashboard

Agricultural raw materials	
Sunflower oil ($/mt)	▼ - 3.7%
Rapeseed oil ($/mt)	▼ - 2.6%
Palm oil ($/mt)	▲ 3.4%
Wheat, US HRW ($/mt)	▲ 2.2%
Maize ($/mt)	▲ 3.1%

Inflation commentary

Trade snapshots

Industry facts and stats



Investment is key to long-term growth

With cost pressures fading and food inflation firmly in low territory, the industry needs now to focus on investment and innovation to ensure long-term growth and food security. For this, it needs to rebuild its margins.

Annual food and non-alcoholic drink inflation was steady at 1.5% in July. This, alongside the June figure, is the lowest rate since October 2021, having seen 15 consecutive months of slowing price rises. Food and non-alcoholic drink inflation has now been lower than UK headline inflation for three months (Chart 1).

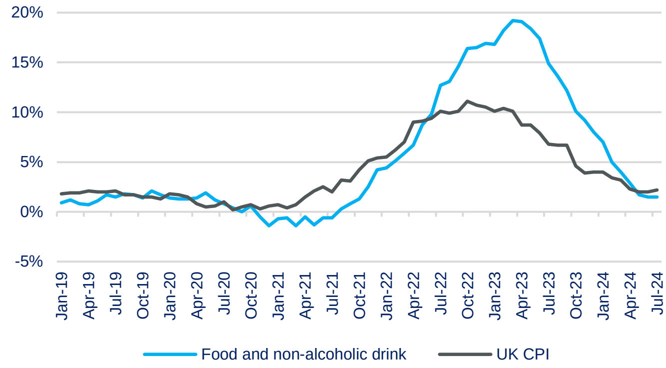
Meanwhile, production costs have been stabilising, with input costs, excluding labour, largely unchanged over the past year (Chart 2). This means that the impacts of the structural shocks of the pandemic and the war in Ukraine on food inflation have now dissipated. Nevertheless, the lasting impact seems to be higher costs throughout the supply chain, which means that we're unlikely to see prices drop. Adverse weather, geopolitics and new EU trade measures on imports (health certificates and check rates at the border) pose risks to inflation.

All of the above seems to indicate that the industry is turning a corner. But for the industry to rebuild from a difficult few years and create sustainable growth, it needs to focus on investment and innovation. Challenging conditions over the last years have meant that businesses postponed or cancelled investment projects and diverted funds to day-to-day operation. As a result, investment in the industry dropped. In 2023, the industry's investment was 30.5% lower than in 2019, contrasting with the UK as a whole where investment was 5.4% higher, and in Q1 2024 it continued to drop.

To invest, businesses need resources, and margins have been eroded. The last four years saw their costs rise at a faster pace than retail prices[1] (Chart 3), which means that producers have absorbed a share of the cost rises. The industry needs to increase volumes, both at home and abroad. With falling exports and household finances still constrained, the road ahead seems quite difficult. Despite recent rises in real wages, about [40% of consumers continue to rein in their spending].

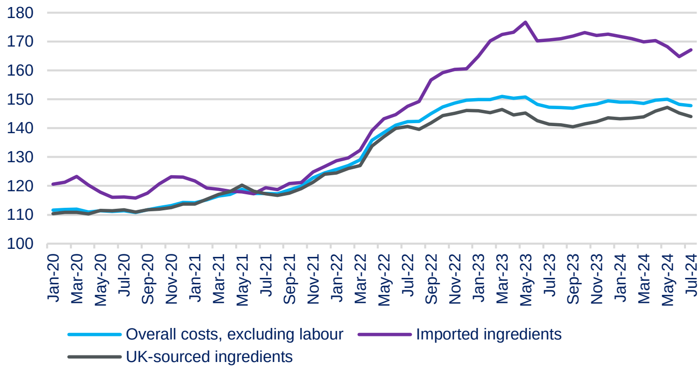
The government's Industrial Strategy will be critical in setting out a long-term strategy for the UK economy and providing stability that will attract both public and private sector investment opportunities.

Chart 1: Food and non-alcoholic drink inflation and UK inflation, July 2024



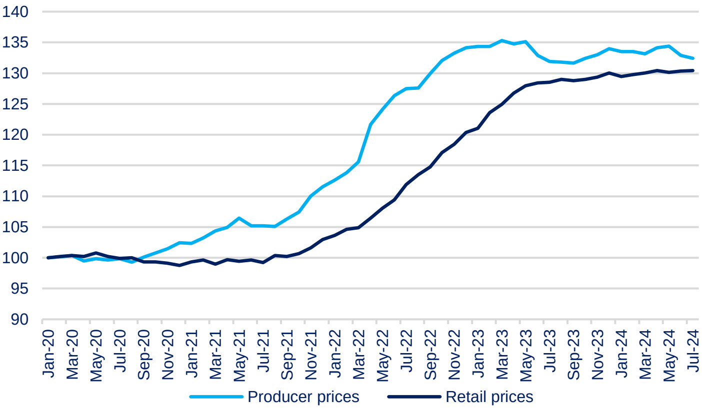
Source: ONS

Chart 2: Manufacturers' costs, Indices, 2015 =100



Source: ONS

Chart 3: Manufacturers' costs versus food and non-alcoholic drink retail prices



Source: ONS

[1] This one-to-one comparison between costs and prices is possible because the indices have been rebased to 100 in January 2020. A similar starting point/ base allows for such comparisons.

Smaller businesses remain under pressure

In Q2, the sector's confidence measured by the FDF net confidence score fell to -6%, the first negative result since Q2 2023 (Chart 4).

Net confidence is calculated as the difference between respondents who perceive business conditions have improved in Q2 from Q1 and those respondents who believe conditions have deteriorated. Businesses that saw conditions unchanged are therefore excluded from this calculation. 56% of businesses believed conditions remained the same, with 19% seeing improved conditions on the quarter, down from 33% in Q1.

Perceptions of market conditions in Q2 differed across business sizes (Chart 5). All large businesses saw a continuation of the conditions experienced in Q1. 58% of mid-size businesses felt the same, while a quarter (25%) felt business conditions had improved. However, SMEs had a net confidence score of -17%, a reversal of the significant improvement in perceptions seen in Q1. This was the main driver behind the decline of the overall confidence score from its record Q1 level, with 39% of smaller businesses experiencing a deterioration.

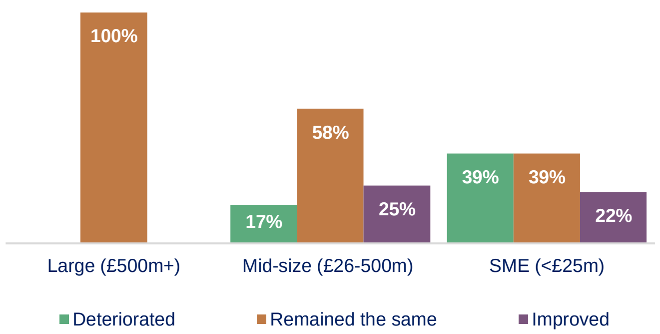
Two thirds of small businesses are worried about demand. This past inflationary episode brought a significant shift in consumption to own-label and cheaper products. And with current real incomes lower than 2019 ones, despite recent pay rises, this behavioural shift is continuing. Smaller producers are the most vulnerable to such market changes, as they produce a limited range of products. Moreover, they typically operate on short-term supply contracts of around four months and on extremely thin margins. Which means that if demand for some of their products drops, they would not have the time and resources to swiftly introduce new products.

The outlook confidence score for Q3 2024 is 6%, with 56% of businesses expecting similar conditions in Q3 as in Q2. Mid-size businesses are the most optimistic with a net outlook score of 17%, with a third (33%) anticipating improved business conditions, compared to 28% of SMEs. All large businesses expect conditions to remain the same (Chart 6).

Chart 4: FDF net confidence score

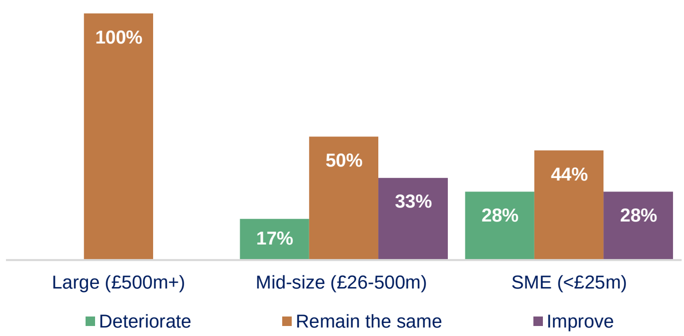
Source: FDF State of Industry Survey

Chart 5: Business conditions in Q2 2024 compared to Q1 2024 by business size



Source: FDF State of Industry Survey
Note: nobody chose 'significantly deteriorated' or 'significantly improved', although these choices were offered.

Chart 6: Expectations about business conditions in Q3 2024 relative to Q2 2024 by business size



Source: FDF State of Industry Survey

Investment intentions bring some hope

Growing sales in the UK market remains the top priority in Q2 for 70% of respondents. Manufacturers have seen their sale volumes fall in the past few years. With food retail sales volumes 6% lower than in January 2020, and a need to grow investment, the industry is focused on higher UK sales.

New product development remains second in terms of growth priorities for over half (52%) of the industry, showcasing the desire of our manufacturers to prioritise innovation and offer a varied range of products, which is crucial for competitiveness (Chart 7).

Automation to address labour shortages and/or improve productivity has increased as a priority. Adopting new and existing technologies will foster greater productivity and help grow the industry. Manufacturers remain resilient in their growth ambitions while facing skill and labour shortages, which we estimate cost the industry around £1bn in lost output in 2023.

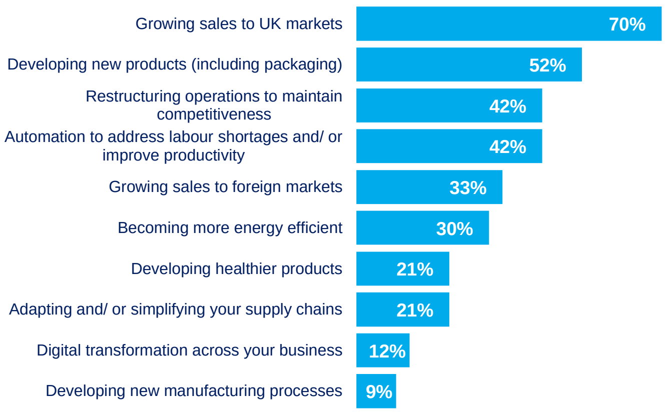
At least half of the respondents are planning to keep their investment expenditure on R&D, skills and training, and buildings unchanged, while over half (56%) are planning to increase their investments in plant and machinery (Chart 8). This is key to the industry rebounding.

However, some factors are likely to continue to limit investment over the next 12 months. Half of the respondents (50%) are limited by uncertainty about demand and changes to the business environment (Chart 9), despite recent improvements in the macroeconomic environment. By size, 80% of large companies and 67% of small businesses were worried about demand.

Uncertainty about upcoming regulation follows closely behind with 47% of respondents. By size, 80% of the large companies, 30% of the mid-sized ones and 61% of the small businesses were uneasy about upcoming regulations. Some specific concerns are about the implementation of the Deposit Return Scheme (DRS) implementation, continued lack of clarity about whether not for EU labelling will be required across the whole GB, and concerns about the proposed Forest Risk Commodities regulation and implementation.

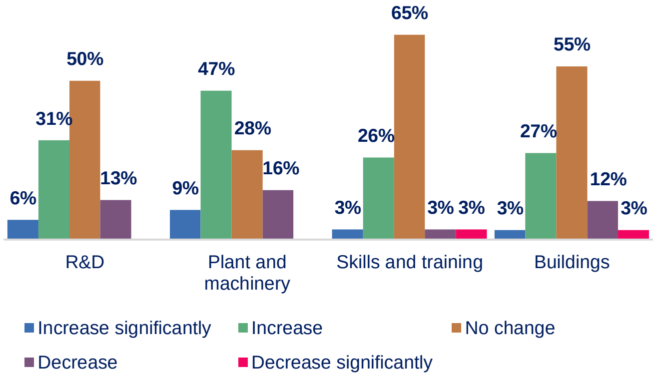
Cost of finance was limiting investment for over a third of the respondents. The Bank of England cut rates by a quarter of a percentage point to 5.0%, the first cut since 2020. With slowing wage rises and decreasing service and core inflation, it's possible that more cut would follow this year, which would help the sector.

Chart 7: Top three growth priorities



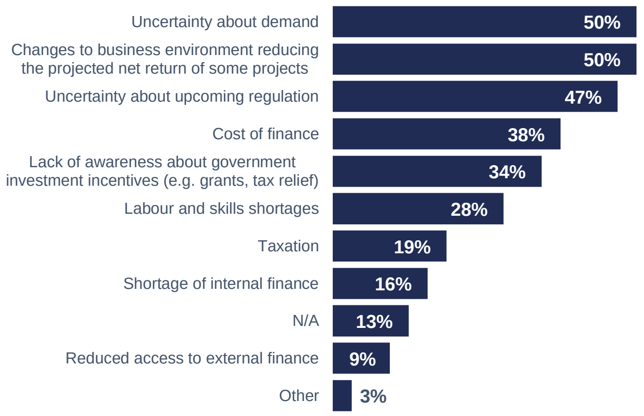
Source: FDF State of Industry Survey

Chart 8: Expectations of planned capital investment expenditure over the next 12 months



Source: FDF State of Industry Survey

Chart 9: Factors limiting investment over the next 12 months



Source: FDF State of Industry Survey

The government should prioritise the UK-EU relationship

A new government presents an opportunity to tackle the challenges and opportunities facing the industry. Half of manufacturers believe that the UK's relationship with the EU should be top priority for the new government (Chart 10). Other major priorities for the industry include employment and skills policies (39% of respondents) and packaging reforms (36%).

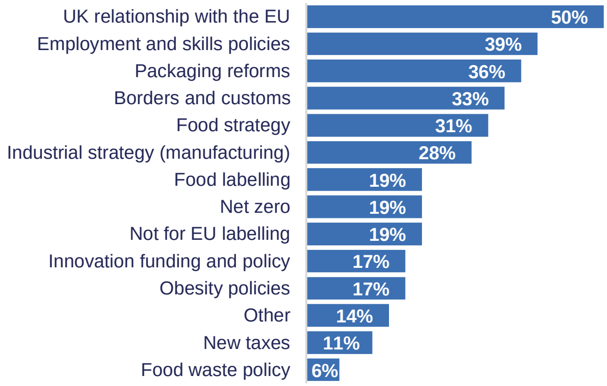
Trade relations are a crucial aspect of the UK's relationship with the EU. Non-tariff trade barriers significantly hinder trade, with administrative costs restricting foreign sales for 54% of manufacturers (Chart 11) and imports for 47% (Chart 12). Additionally, export health certificates pose challenges for 40% of businesses, while import health certificates affect 24%.

SMEs are particularly burdened by these additional costs. With lower sales volumes, they incur higher per-unit costs of complying with export requirements than larger businesses. And, with fewer resources, it's harder for them to manage the necessary paperwork. A lack of awareness of export guidance is the second most significant barrier to export for 40% of manufacturers. 21% of manufacturers face issues importing due to a lack of guidance.

The Common User Charge exemplifies the lack of guidance. Starting 30 April 2024, the government has imposed a charge on all eligible imports entering the UK through the Port of Dover and Eurotunnel. This is a flat fee designed to fund government operations at these locations. However, these charges will be collected in arrears with the first invoices issued in August. There is no way to track charges incurred on a rolling basis in real time, making it difficult for businesses to budget for these expenses. SMEs who tend to import via mixed consignments will be particularly impacted, with 71% unaware of the fees. Overall, 57% of respondents were unsure of the charges.

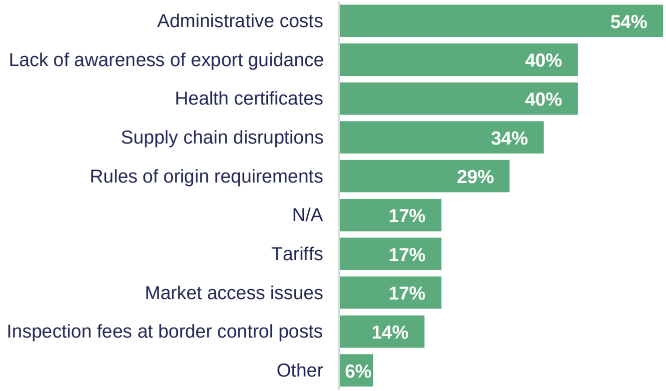
Food and drink trade has been declining recently, both in value and volume terms, with these regulatory obstacles contributing to the drop. For instance, products measured in kilograms saw export volumes decline by 20% in Q1 2024 compared to Q1 2023, reaching the lowest Q1 level seen in the past 15 years, excluding the pandemic. This decline in exports is not a blip. Average UK's export volumes between 2020 and 2023 were 23% below the 2015 – 2019 average. By destination, export volumes to the EU fell by 27%, compared to an 8% decline to the rest of the world. It's not surprising that 33% of respondents are prioritising growing their foreign sales (Chart 7), a significant share, as not all manufacturers are exporters.

Chart 10: Top policy priorities with the new government



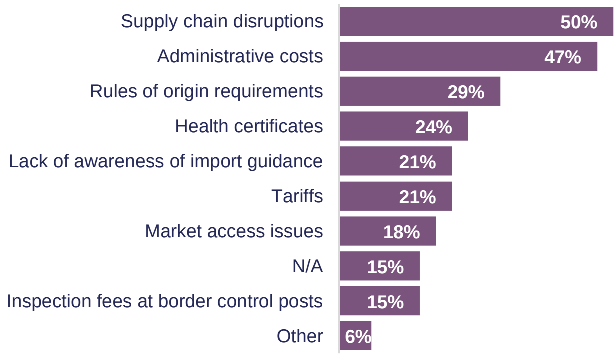
Source: FDF State of Industry Survey

Chart 11: Top export barriers



Source: FDF State of Industry Survey

Chart 12: Top import barriers



Source: FDF State of Industry Survey

Training and UKRI funding could address labour shortages

Labour shortages in the sector were broadly unchanged in Q2, with vacancy rates now at 4.9% from 5.0% in Q1 (Chart 13), above those in wider manufacturing and the UK, at 2.6% and 2.8% respectively.

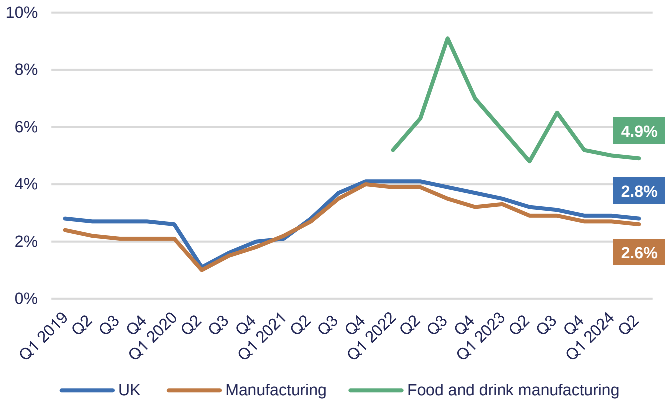
Labour shortages have been a long-standing structural issue for the industry. It's therefore not surprising that the sector thinks that employment and skills policy should be a priority for the new Government (Chart 10). Food and drink manufacturers are seeking reforms to the UK skills system including Apprenticeships to ensure that it delivers the right skills for now and the future. As good employer, the industry supports the intent behind the new government's plan to implement its 'Making Work Pay: Delivering a New Deal for Working People'.

Just under a half of manufacturers (45%) reported vacancies of 0 to 5%. We estimate the vacancy rate of SMEs at 6.4% on average, higher than that of large businesses (3.8%) or mid-size businesses (3.4%). Unfilled vacancies continue to affect a wide range of roles and skills. This includes: **high-skilled workers** (software development, automation, quality assurance and engineering), **technical specialists** (engineering technicians, sales) or **production operatives** (agricultural workers, cleaning roles).

Food and drink has only recently been recognised by the UK government as a strategic advanced manufacturing sector. This recognition will ensure government policies and programmes such as UK Research and Innovation (UKRI) funding is aligned to key sectors. 58% of manufacturers would like funding prioritised for novel and alternative packaging, and 55% for resource footprint measurement and reduction (Chart 14). This will help manufacturers innovate and adopt new and existing technologies, of which both have been stifled by persistent labour and skills shortages.

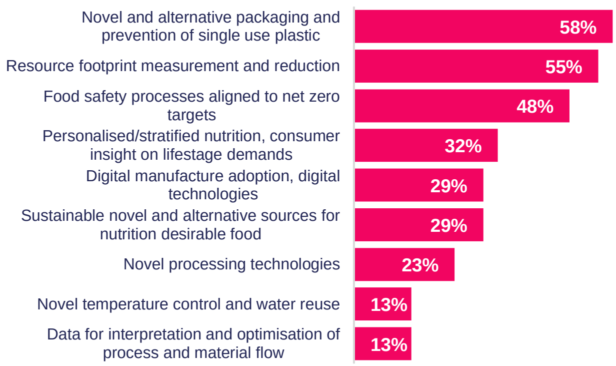
The new government's proposals to create a Growth and Skills Levy in place of the current Apprenticeship Levy will help employers to invest in and develop the right skills for their workforce. With greater flexibility to spend up to 50% of levy funds on non-apprenticeship training including modular courses, 62% of respondents would invest funds in first line manager development, and 56% for both business improvement techniques and engineering conversion modules to upskill (Chart 15). When considering accredited compliance training courses, food safety training was the most popular choice, with 70% of responses. Apprenticeships and non-apprenticeship training courses would upskill new and existing employees, and help address the skill and labour shortages that are so prevalent in the industry.

Chart 13: Vacancy rate in UK, manufacturing and food and drink manufacturing *(vacancies per 100 employees)*



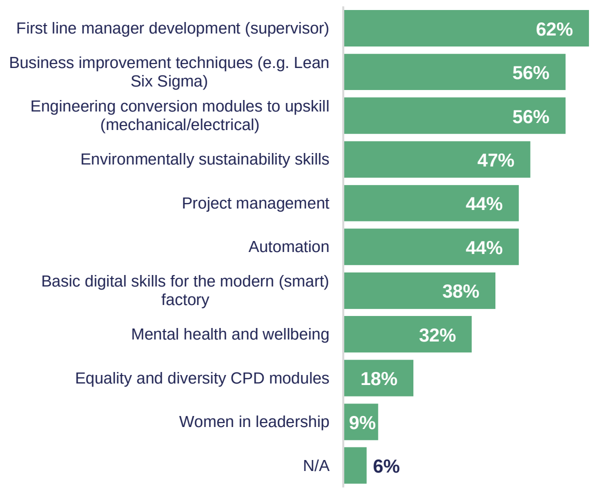
Source: FDF State of Industry Surveys and ONS

Chart 14: Areas of potential funding from UKRI



Source: FDF State of Industry Survey

Chart 15: Modular training courses with apprenticeship levy funds



Source: FDF State of Industry Survey

Cost inflation is slowing, but some pressures persist

On average, total production costs increased by 5.4% over the year to June, while selling prices rose by 3.9%. Cost rises of over 10% were still experienced by 19% of manufacturers, below last quarter's figure of 28%. In contrast, costs fell for 6% of respondents (Chart 16). SMEs saw the highest increase in their costs, with an average of 7.2%, compared to 5.6% and 4.4% for large business and mid-size businesses respectively.

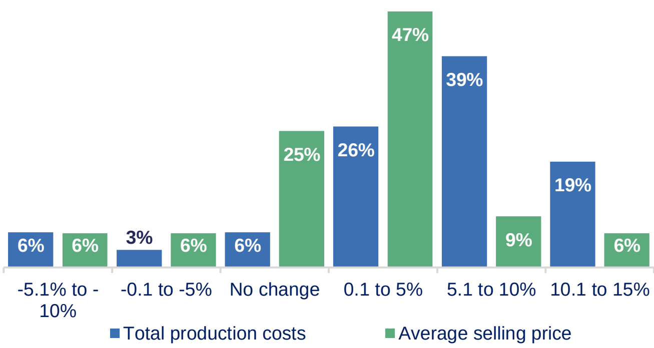
In terms of prices, 6% of respondents stated their average selling prices rose by over 10%, compared to 9% in Q1, and a quarter (25%) in Q4. Meanwhile, 12% of manufacturers saw a fall in their average price. Large businesses had the greatest increases in their average price at 4.5% on average, compared to 0.8% and 2.1% for mid-size and small businesses respectively. Smaller businesses find it harder to pass on their cost increases through prices due to their limited bargaining power.

These figures diverge from the ONS statistics on costs. The ONS data does not include labour costs, which pose significant pressures to smaller producers in particular. Also, our sample includes more smaller respondents which represent 97% of our sector.

For the year to June 2025, manufacturers expect their costs to rise by 2.9% and prices by 1.0%. Notably, 61% of manufacturers expect production costs to increase by 0.1 to 5% and 39% expect no change in average prices (Chart 17).

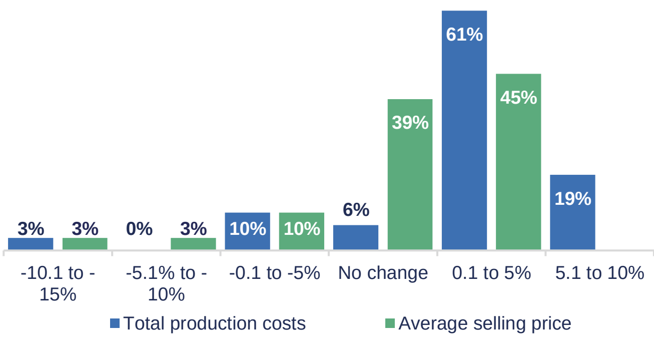
Just over a third of manufacturers (35%) increased their output in the year to June 2024, in contrast to the 63% that said theirs increased in the Q1 survey (Chart 18). A similar proportion (32%) had seen a contraction in their output. Broken down by business size, a larger proportion of smaller businesses saw a contraction, with 45% compared to 20% for large businesses and 18% for mid-size. Looking ahead, 59% are expecting growth in their business, while only 15% are expecting a reduction.

Chart 16: Changes in total production costs and average selling price over the year to June 2024



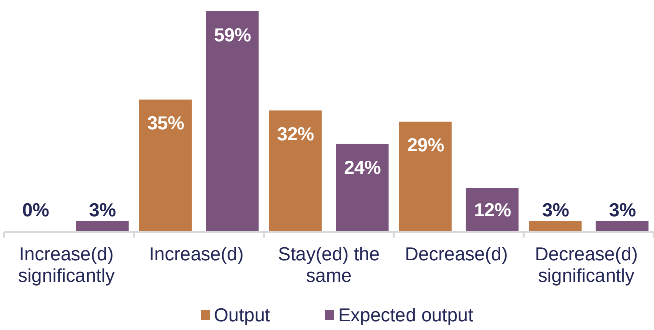
Source: FDF State of Industry Survey

Chart 17: Expected changes in total production costs and average selling price over the year to June 2025



Source: FDF State of Industry Survey

Chart 18: Output changes in the year to June 2024 and expected output changes over the next 12 months



Source: FDF State of Industry Survey

Who responded?

There was strong representation from the industry, with companies from all turnover bands, all employment sizes and from a wide range of industry sub-sectors.

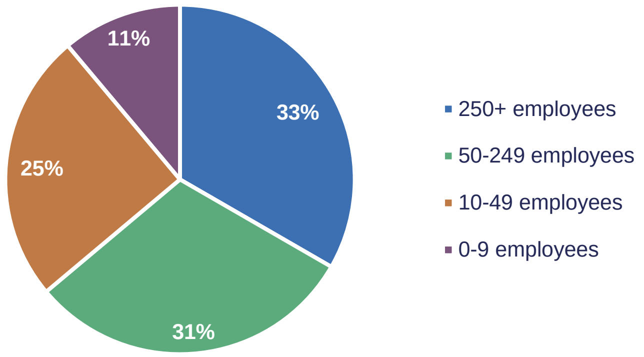
A third (33%) of the businesses surveyed are large employers with more than 250 employees, while 31% are businesses with 50-249 employees, and 25% small businesses with 10 to 49 employees (Chart 19).

By turnover, 28% of respondents are small businesses with a turnover of £5m or less, while 17% are businesses with a turnover exceeding £1bn (Chart 20).

Businesses also represent a wide variety of sectors (Chart 21). The best represented ones were bakery, soft drinks and grain/starches. The 'Other' category covers businesses operating in sectors such as organic ambient grocery, vegetable seeds, crisps and snacks, and cereals.

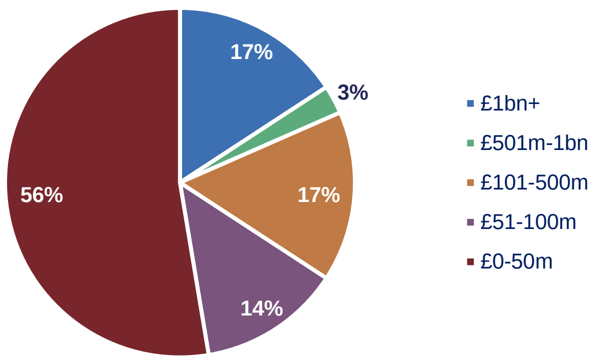
78% of manufacturers operate in England, while a third (33%) have production facilities located in Scotland and 14% in Wales.

Chart 19: Respondents by employment size



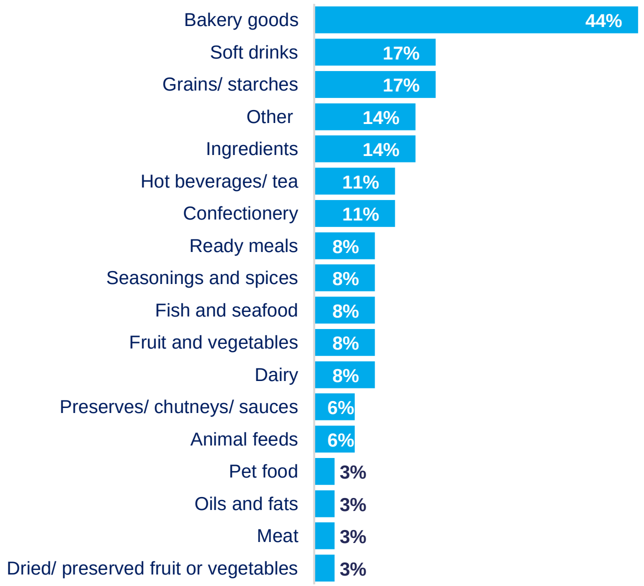
Source: FDF State of Industry Survey

Chart 20: Respondents by turnover



Source: FDF State of Industry Survey

Chart 21: Respondents by sub-sector



Source: FDF State of Industry Survey

About the FDF

The FDF is a powerful voice for the UK's vibrant, resilient and diverse food and drink manufacturing industry. For over 100 years, we have successfully contributed to policy making and legislative development, championing our members' views – large and small – on the critical issues of the day.

We bring together business, government and stakeholders to ensure our manufacturers have the right conditions to grow, invest and employ, while continuing to produce high quality, nutritious and affordable food and drink. With more than 1,000 members – from the most recognisable global brands to the most innovative start-ups – we represent the largest manufacturing sector in the country.

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