Appendix A: Evidence and findings for individual product categories

A.1 We have reviewed the financial performance of food manufacturers, using information provided in their responses to our voluntary requests for information, as well as publicly available financial statements.[1,2]

A.2 The analysis is based on data covering UK sales of products within our chosen product categories, rather than their overall business which may encompass several products or multiple countries.[3] In some cases, a single manufacturer may produce a number of brands within a given category – for example, a pet food manufacturer might produce multiple brands of cat food and multiple brands of dog food. Some manufacturers also produce products in more than one of our ten product categories, in which case they are included separately in each.[4]

A.3 We have compared historical profitability to the latest available comparable information (either 2022 or 2023 financial year). Specific time periods vary by manufacturer due to differences in financial year ends. For the purposes of this analysis, financial years are referred to as the calendar years to which they are most closely aligned: for example, year-ending March 2022 is referred to as 2021; year-ending September 2022 is referred to as 2022.[5] We comment on trends without identifying individual manufacturers, and in some cases show anonymised manufacturer data. We have excluded from this appendix confidential financial information which has been provided by Parties on a voluntary basis.

Infant Formula is a high margin category that has generated increasing unit profits for manufacturers

A.4 Infant formula manufacturers have among the highest margin levels, as a percentage of revenue, of manufacturers across all product categories that we have considered.

[1] We refer throughout the report to 'food manufacturers' for simplicity. This includes businesses with a range of different business models, including manufacturers, processors, and, in some cases, distributors. Where comparisons are made, care has been taken to ensure that they are between comparable businesses, for example excluding distributors from comparisons of levels of profitability.
[2] The information available varies by manufacturer, due to both differences in reporting and differing levels of detail supplied. For example, some manufacturers have different approaches to tracking product profitability, including different approaches to cost allocation. In addition, some manufacturers provided us with detailed volume, unit pricing, and unit profitability metrics, whereas others did not. The data cited in this appendix is illustrative of our findings and the amount of commentary provided differs across different product categories.
[3] For publicly available accounts, we have included only manufacturers for whom UK sales of the relevant category are the primary focus of the manufacturer.
[4] Where manufacturers produce multiple products, or branded and own-label, they are treated as a unique manufacturer in each category, meaning for example, if a manufacturer made branded beans, own-label beans, and branded ready meals, it would appear three times (twice in beans, once in ready meals).
[5] In one case, year end is June. In this case, FY ending June 2022 is referred to as 2022.

A.5 Manufacturer price rises have been significant in recent years. This has contributed to material increases in profit per unit for some manufacturers. For these manufacturers, profit as a share of revenue increased in 2022 but has come down in the first half of 2023. Current profitability as a share of revenue is either below or broadly in-line with historical levels.

A.6 For Kendamil, a relatively recent entrant into the market, public accounts show that profitability has been increasing. Kendamil's net profit was 4.1% of revenue in FY20, 12.4% in FY21 and 19.7% in FY22. Kendamil grew absolute profits from £1.0m in FY20 to £6.7m in FY22.[6]

Baked beans is a high margin product category which has seen rising prices and unit profitability since 2021, but in which declining volumes have reduced absolute profits for brands

A.7 Branded and own-label baked beans manufacturers have increased prices to retailers significantly in recent years. All manufacturers have increased prices by a similar amount in recent years - by around 10% between 2018 and 2021, and by 20 to 40% between 2021 and 2022.

A.8 This has in part been driven by significant input cost inflation, in particular higher costs of packaging (primarily metal for tins); food ingredients (eg beans, starch, tomatoes); and manufacturing (especially energy) as explained in section 2.

A.9 However, per unit, prices have risen by more than production costs, leading to increases in unit profitability (profit per kg or unit).[7] One manufacturer told us that increasing unit profitability offset increases in other costs including wages and interest payments. For some manufacturers, profitability increased as a percentage of revenue in 2022, and for others it declined. Both branded and own-label manufacturers remained broadly within normal ranges of net profitability when compared with recent performance.

A.10 Branded manufacturers of baked beans have had declining profits or sub-inflationary profit growth since 2021. Own-label beans manufactures have increased profits, although for some manufacturers this represented a recovery from a low in 2021 to levels more consistent with pre-Covid averages.

[6] Source: Kendamil's public accounts. March Year End (FY22 = year to March 2022). More recent Kendamil figures unavailable
[7] 'Per unit' refers to per kg, per case or per tin depending on the available information.

Pet Food is a relatively high margin category in which manufacturers have increased unit profits, with mixed results for sales volumes and absolute profitability

A.11 Profitability levels of branded and own-label manufacturers of pet food are broadly comparable to those active in the markets for infant formula, beans, and mayonnaise.

A.12 Pet food manufacturers (in our sample) have increased their unit prices (price per kg) by 20 to 30% since 2021. This has contributed to rising unit profits of 5 to 20% over the same time period.

A.13 However, pet food manufacturers have made less profit as a percentage of revenue than in previous years. All manufacturers that we reviewed had declining profit as a percentage of sales in the latest year.

A.14 Volume trends varied, with some (especially the more premium branded manufacturers) losing volumes, and others (especially own-label manufacturers) growing volumes materially. However, due to price rises, all manufacturers grew revenue.

A.15 Only one manufacturer reviewed managed to increase its absolute profit by more than CPI inflation. Others either had declining absolute profits, or a rate of profit growth less than CPI inflation over the relevant period.

Mayonnaise is a relatively high margin category, with varying recent manufacturer performance trends

A.16 In mayonnaise, data availability and commercial sensitivity restrict the detail on which we are able to report on profitability dynamics.

A.17 In general, although price rises have been significant, there has been no evidence of concerning levels of growth in profitability for any manufacturer.

A.18 Overall profit levels have had varying trajectories. Evidence does not suggest material growth in profit levels in the category.

Ready meals is a relatively low margin category which has shown some evidence of declining margins

A.19 Ready meals is a relatively low margin product category, with recent typical manufacturer net margins less than 5%. This is consistent with it being largely own-label. In the years since 2020, the average net margin for the main own label manufacturers was 3.9%.

A.20 In the last two years, there has been some evidence of declining profitability.

(a) Between 2021 and 2022, revenue for Greencore, Bakkavor, and 2 Sisters combined increased. From 2021 to 2022, absolute net profit grew at a level significantly below CPI inflation. Their combined margin as a share of revenue also declined in 2022. Available year-to-date financials show further decline in net profit as a percentage of revenue in 2023.

(b) The public accounts for Oscar Meyer, another large own-label ready meal manufacturer, show declining profit. Net profit fell from £8.7m in 2020/21 (2.8% of revenue), to a loss of £10.4m (-3.3% of revenue) in 2021/22.[8]

(c) Bigham's is a premium, niche manufacturer of branded ready meals. Their public accounts similarly show a decline in profit. Net profit fell from £8.4m in FY2020/21 (8.1% of revenue) to £5.0m (4.2% of revenue) in 2021/22.

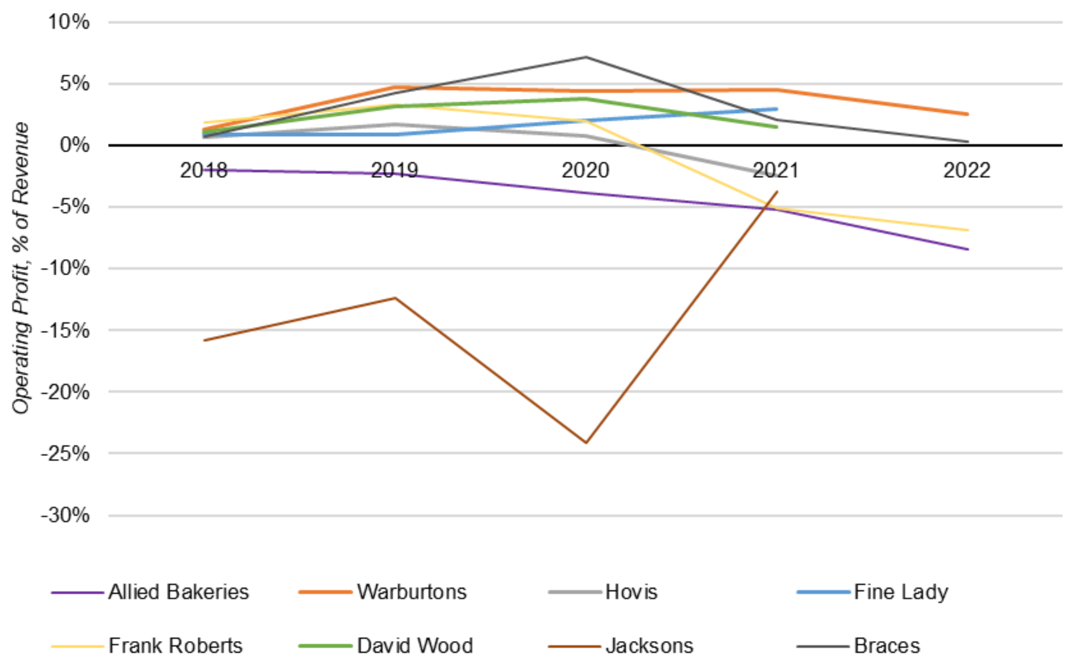
Bread is a low margin category that has seen further margin decline since the start of the recent inflationary period

A.21 Bread is a low margin category. Public financials show that net profit for bread manufacturers is typically below 5% of revenue. It is common for manufacturers to make a loss in this category: Allied Bakeries, Frank Roberts, Jackson's and Hovis have all had negative net profit in their latest publicly reported financials. Jackson's was acquired in September 2023, to avoid going into administration.[9]

[8] OSCAR MAYER LIMITED filing history - Find and update company information - GOV.UK (company-information.service.gov.uk). March year end.

[9] Acquired by Allen Jackson Bakery Ltd, a Newco, part of Lifft Group Jacksons the Bakers acquired by Allen Jackson Bakery Limited (foodmanufacture.co.uk)

Figure A.1: Bread Manufacturers Publicly Reported Operating Profit , 2018-22



Source: Companies House. Where relevant, excludes exceptionals.

A.22 There is evidence of profitability declining further in recent years. All but one manufacturer made a lower net profit (or higher net loss) in their latest reporting year compared to the previous year, both in absolute terms and as a percentage of revenue. There is also evidence of declining unit profitability (ie profit per loaf) in 2022.

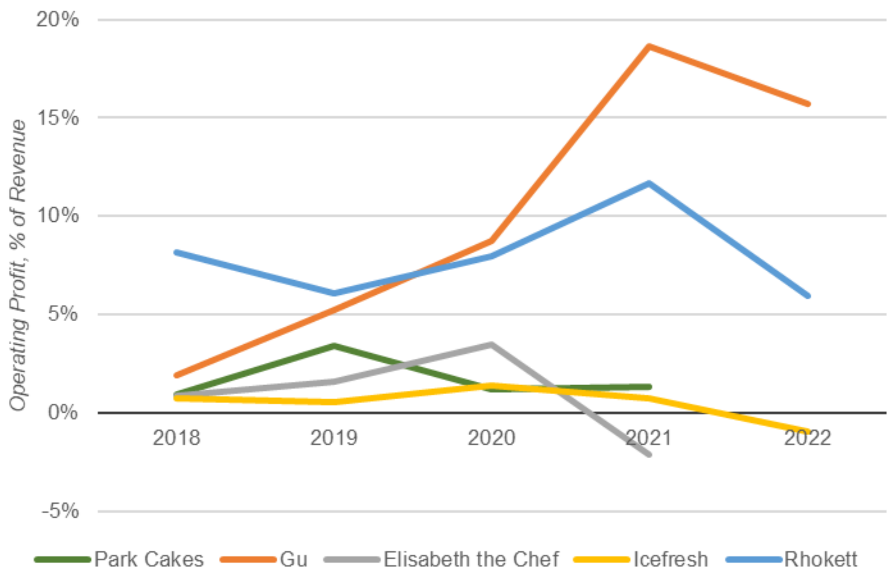
Chilled desserts is a relatively low margin category and evidence suggests that profits have recently declined.

A.23 Chilled desserts is, in general, a low margin category, consistent with being largely own-label. Most manufacturers consistently make less than 5% net margin.

A.24 Some niche premium branded players command higher margins (Gu, 15.7% net margin in FY22, Rhokett 5.9% net margin in FY22). However, these form a small segment of the market and are relatively small players; in FY22, the combined revenue for premium manufacturers Gu and Rhokett was less than £100m, whereas mass market manufacturers Muller, Bakkavor, and Park Cakes combined had close to £1bn desserts revenue in 2022.[10]

[10] Companies House

Figure A.2: Chilled Desserts Manufacturers, Publicly Reported Operating Profit , 2018-22



Source: Companies House.

A.25 In 2022, margins as a percentage of revenue fell among all manufacturers for whom data is available. In 2022, Rhokett, Icefresh, Gu, Muller, and Bakkavor all showed declining net profit as a percentage of revenue.[11] Available data also suggests that manufacturers have reduced their unit profitability. Despite near universal revenue growth in 2022, all chilled desserts manufacturers had declining net profit in absolute terms.

In lemonade profitability trends have varied, but overall profits appear to have fallen since 2021

A.26 Since 2021, both branded and own-label lemonade manufacturers have materially increased their prices (to retailers). Net revenue per unit (ie per litre or case) increased by approximately 10 to 25% for all manufacturers.

A.27 Unit profitability trends have varied. Some manufacturers have increased their profit per litre,[12] whereas for others, profit per litre has decreased (ie manufacturers have absorbed part of their cost inflation). For most manufacturers, profit as a percentage of revenue has declined since 2021.

A.28 Some manufacturers have managed to grow volumes modestly (only one grew volumes by more than 5% between 2021 and 2022). By contrast, for some manufacturers, volumes have declined significantly (multiple manufacturers lost over 10% of volumes between 2021 and 2022).

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[11] Companies house

[12] Or other volume metric used, eg case/case equivalent.

A.29 There has been a mix of trends in absolute profit, reflecting variation in unit profitability and volume trends, but overall, profits appear to be in decline. While some manufacturers grew profits in nominal terms in 2022, only one grew profits at a rate above CPI inflation, and there has been evidence of profitability falling further in 2023 year-to-date.

Milk is a low margin category that experienced declining profit in 2022

A.30 Milk is a low margin category, consistent with it being a commodity product with limited product differentiation, dominated by own-label manufacturers.

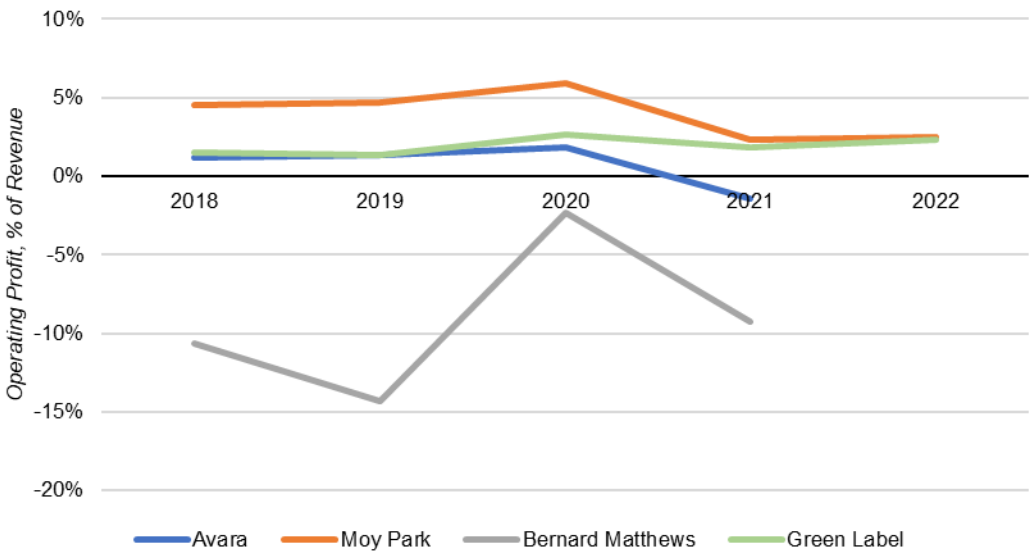
A.31 In 2022, manufacturer milk prices (net revenue per litre) were around 20% higher than in 2021.

A.32 Despite this, milk manufacturers have experienced lower profitability. In absolute terms, as a percentage of revenue, and per litre of milk, large manufacturers had declining profit levels. This implies that dairies have been unable to pass on their rising costs (which are primarily liquid milk, which is around two-thirds of cost, also packaging, processing, and logistics).

Poultry is a low margin category with all manufacturers making consistently low profits

A.33 Poultry is a low margin category, consistent with its limited brand presence and lack of product differentiation. Since 2018, only one manufacturer has made more than 2.5% net margin in any year (Moy Park, 2018/20, with margins since coming down).

Figure A.3: Poultry Manufacturers, Publicly Reported Operating Profit, 2018-22



Source: Companies House.
Notes:
(1) Financial years are aligned to align with majority of the year (eg Avara FY22 ends May 2022 and so is aligned to 2021 in this Figure).
(2) Avara continuing operations; Moy Park excludes restructuring costs.

A.34 Some manufacturers have had declining profitability since 2021 (both in absolute and as a percentage of revenue) and, while others have had increased profitability, none has achieved net margins in excess of 2.5%.