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Quarterly Briefing Report

Q3 2021 July - September

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Introduction

I launched the Quarterly Briefing Report to satisfy the widespread need for factual information about what has happened recently in foodservice and its supply chain and how things will pan out over the short term. At the start of the covid lockdown I launched my free Weekly Briefing Report and more recently my Monthly Briefing Report which, with my Quarterly Briefing Reports, is now available as a premium subscription service.

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Headlines

I am unsure about the reasons behind the "big" issues afflicting foodservice and the wider economy, by which I mean: inflation and shortages of workers. On the one hand, it is possible to just say "que sera" (for those not around in the 1950s, that was the title of a Doris Day record / tune / chart-topper: "Whatever will be, will be"). But on the other hand, knowing, or having a good idea of, the reasons might lead to more informed decision-making.

Various reasons are given for worker shortages: Brexit is usually top of the list followed by: people have stopped wanting to drive trucks / work in hospitality; working in an Amazon warehouse is preferable to doing whatever they did before; living on the dole brings in more income than actually working. To each of these there is an objection: if Brexit is important, how come there are shortages in the USA? If people topped wanting to drive trucks, surely their numbers will show up somewhere else in the economy? Working in an Amazon warehouse might be great but only about 50,000 work there in the UK, and only 10,000 new roles have been added this year – there are ten times as many truck driver vacancies.

I'm not saying these reasons are without value, it's just that individually, and even jointly, they don't seem to explain why there aren't enough people to go round.

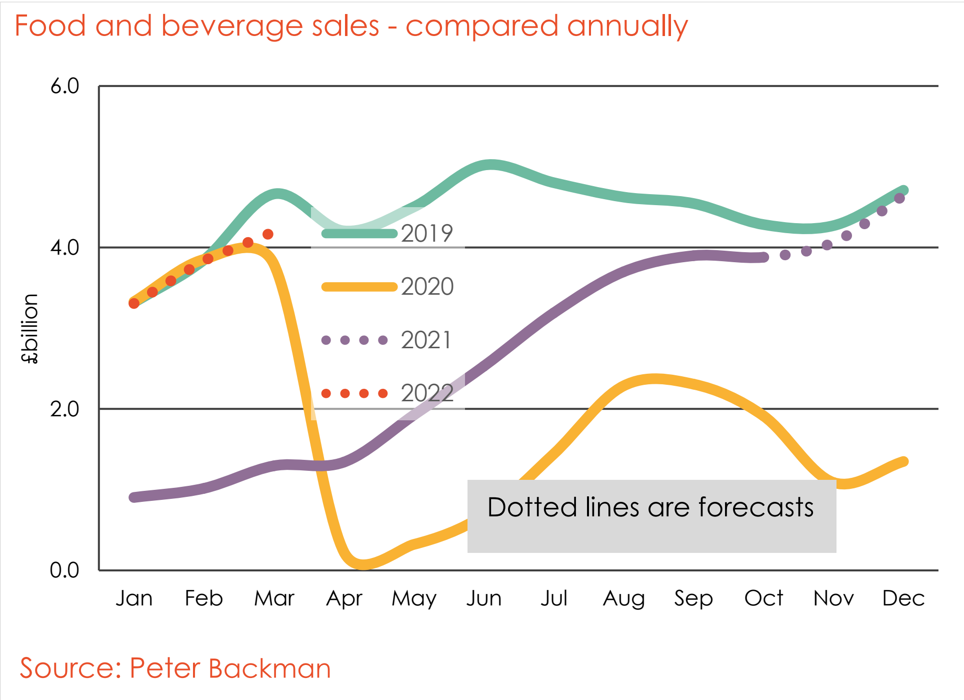
And the same applies to inflation. Is it due to Brexit? Or demand from elsewhere (supermarkets competing with coffee shops for supplies of muffins)? Or shortages of individual products (because of crop failures, inadequate numbers of workers in abattoirs, or something else)?

Although there are objections to each of these (for example: Brexit doesn't wash, because inflation is higher in Europe and the USA than in the UK at the moment), but there may be more to these arguments in respect of product shortages and demand from elsewhere driving up inflation generally – and for food in particular. That would suggest there is a scrabble for supplies which, in turn, implies some form of "panic buying" not only by the general public but by businesses throughout the supply chain. If so, the panic is not at elevated levels – not for now anyway.

But we should be on the lookout for real panic buying in the supply chain, leading to higher levels of inflation baked into the economy. If that takes hold, all bets are off. But in my forecasts, I am assuming sanity accompanied by some relatively high inflation for the next few months. I hope it's no worse than that.

What happened this time last year?

- Once again, the foodservice sector was standing on the edge of a precipice – with the impending impact of lockdowns affecting trading across the sector.
- Total lockdown was to come into force on 5 November for at least a month, possibly longer, including a prohibition on restaurant and pub trading other than for delivery and take away,
- Lessons learned by the scientific fraternity were being applied to medical interventions, with the result that there were grounds for hope that covid would be defeated (or at worst, minimised)
- The general mood of the public was becoming fractious with the result that issues surrounding social distancing, and hygiene, were not being taken as seriously as perhaps required.
- For the foodservice sector specifically, there were plusses and minuses. But it wasn't totally uncharted territory - operators had learned how to do things during lockdowns in the past six months and began to know what to expect.



- Delivery and take away were much in demand from customers
- Businesses in the foodservice sector had been weakened by debt (rent, workers, and unpaid VAT) and a loss of confidence.
- The Job Retention Scheme (the original furlough scheme) was to be replaced by the less generous Job Support Scheme; consequently jobs were being made redundant, staff were being let go, businesses were failing, and confidence was falling.

Review of the past month

I normally provide several paragraphs about the past month. But October was fairly subdued.

Two of the biggest issues were the increase of VAT in hospitality from 5% to 12.5%, and the ending of the furlough scheme, both of which took place on 1 October. But there was little overall immediate effect from these two, potentially significant, changes. I suspect that their impact will emerge over the next few months

Most operators took the hit (or most of it) from the VAT increase – I'd note that they did not reduce prices when the rate came down in the summer of 2020 (nor was that the government's intention at the time). But they will have to cope with the impact on their balance sheets of rising VAT payments without a commensurate increase in prices.

The ending of the furlough scheme probably had little impact on the hospitality sector because most furloughed staff had either been brought back on to the payroll, or had been let go, or had found another job. The wider impact of the ending of furlough is that several hundred thousand people have been brought back into the workplace or have been made redundant. Either way, this would imply a potential pool of labour from which hospitality (and many other sectors) might be able to find employees. The extent to which this is happening is muted, possibly because the people in this pool do not have the skills (or motivation) to work in hospitality.

This highlights the other big issues that face the hospitality sector – and which were at play for some time (not merely in October). These issues are labour shortages, supply shortages and incipient inflation.

Despite these negative headwinds, demand in the discretionary parts of the market (restaurants, QSR and pubs) continued to expand. Even the hotel and leisure sectors grew.

While in no way a "normal" month there were signs of activity in what had become a very fearful sector over the prior year and a half.

Quarterly Review

July to September 2021

The summer quarter was also positive following so-called "Freedom Day" (delayed by a month to mid-July) which in effect gave permission for the population to start to return to normal patterns of eating out. This was not evenly spread across demographics and regions – but the overall effect was to build on the positive moves since selective restrictions were eased, first in mid-March followed by a second tranche in mid-April.

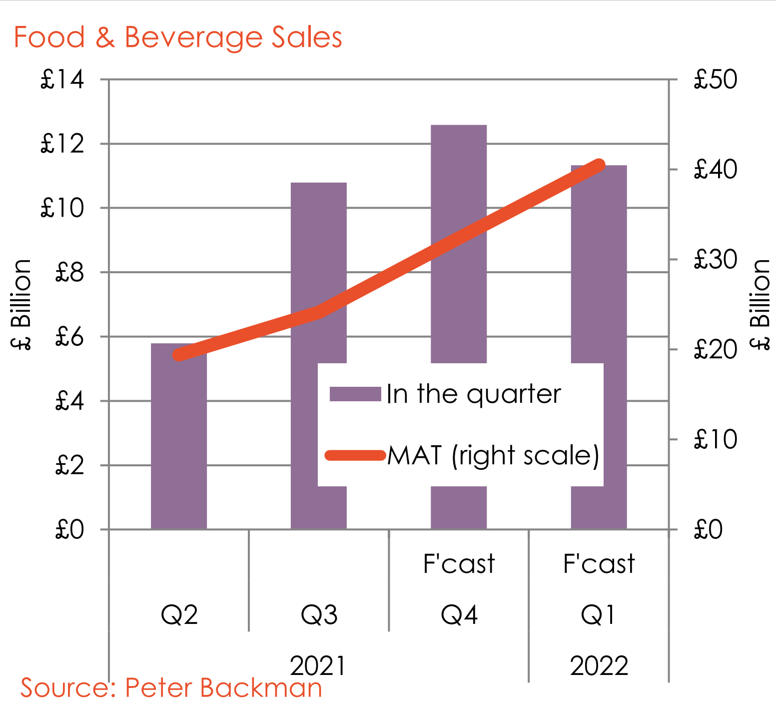
The "pingdemic", which had disrupted so much of the hospitality sector through reducing the potential numbers of guests and workers (because many had to isolate), was got under reasonable control towards the end of the quarter.

At the same time, the growing rate of vaccinations was slowing down the covid "numbers" (cases, hospitalisations, and deaths). And the holiday season arrived.

Because travelling for overseas holidays was not awkward (because of the requirement to be tested and the choice of destination was restricted) many Brits decided to holiday in the UK. And that gave rise to a boom in staycationing activity which included: hotel business; self-catering (via Airbnb and other channels); holiday parks; caravanning; and staying with family and friends. This gave rise to a growth in eating out (in restaurants, cafes, take ways) significantly above what would be expected in a "normal" year.

So there was really positive news. But it wasn't spread evenly across the UK; regions that usually do well in the summer (London and other destinations popular with overseas tourists) gave way to seaside resorts (notably in the south west) and country locations.

This was a repetition of the "shape" of hospitality demand in 2020 – albeit at a higher level - on the back of enhanced consumer confidence that it was OK to get out and about. I suspect there will be echoes next year too – but I also expect overseas holidays to start getting back to something approaching "normal" in 2022.



Source: Peter Backman

Thus, the summer was good for many hospitality destinations – but not all, and in particular those in London or dependent on overseas visitors, saw massively reduced levels of business.

Meanwhile schools were running with lower pupil numbers than in a normal year because of high levels of covid cases and the consequent requirement for whole classes, and year groups, to isolate involving large numbers of pupils and teachers. However, school meals are not generally a major feature of the summer period since schools are only open for a few weeks in July. And by the time the end of the holiday period came round in September, the high levels of isolating pupils and teachers had been substantially reduced.

There was trepidation over the return of workers, generally, following the end of the holidays. Would people continue to work from home and importantly what would the numbers look like for those returning to their offices? In the end, September failed to produce definitive answers and the full extent of changing work patterns induced by covid still remains to be seen (and, I suspect, is likely only to be truly apparent over the next couple of years).

Inflation

Headline CPI inflation in September was 2.9% (slightly down on August) compared with a year earlier.

According to ONS, restaurants increased their menu prices by an average of 6% in September – but that was much lower than the August figure of 21% which was heavily influenced by the reduction of -7% a year earlier when the Eat Out to Help Out scheme was in operation. Incidentally, I don't recall comments at the time about the prices being reduced.

While selling prices were being marked up, some food costs were also on the rise. Oils and fats saw an increase of 11% in September (up from 8% in August), milk products increased 7% (versus 3% in August) and lamb increased 4% in September (down from 6% in August). This rise in oil prices reflects significant global increases in vegetable oil prices driven by growing demand for biodiesel accompanied by unhelpful weather in growing areas. Also globally, sugar prices were on the increase arising from frost damage in Brazil. These global changes are becoming threatening and have already lead to a 33% increase in global food prices recorded by the UN Food and

Agriculture Organisation in September. These increases are being driven by the rising cost of fuel (used for growing and transporting food); additionally, labour shortages around the world have helped push up the cost of harvesting, processing, and distributing food. And the increasingly changeable weather has increased volatility in food yields.

All in all, the cost of food is set to rise during the forecast period. The challenge for foodservice operators is to contain these increases, whenever and however possible, and should price increases be necessary (which they certainly will be), will customers pay the increase? Or will they change their purchasing patterns – or even shun eating out entirely? Past history suggests they will do all of these things but the extent to which they do anything will depend on many issues such as: demographics, meal price, location, service type, and more.

International visitors

About 3.5 million passengers passed through Heathrow in September – 28% of the level in September 2019; the good news is that numbers are rising – there were fewer than half a million passengers just six months ago. From this we can conclude, in view of easing restrictions on entry into the UK from some countries, numbers of overseas visitors are likely to rise. But during the forecast period over the next six months, I would be surprised if they were even at half "normal" levels. This is bad news in particular for hotels that depend on business travellers.

Working from Home

We will start to see how Working from Home pans out – Will it be a hybrid model (two days a week in the office, three days at home)? Who will it affect? How will it play in London, and other cities?

For now, it's too early to see what is happening. Figures from TfL shed some light on this, but they don't yet cover September – the month when people returned from holidays and when, general comments suggest, new working from home / office working practices should start to become clearer.

But TfL figures show that total numbers of passengers on the system in August were 58% of those in August 2019. In general, changes in passenger numbers in each mode of travel (bus, tube, DLR etc) were broadly similar over the period – but with passengers on buses outperforming the average and tube passenger numbers underperforming.

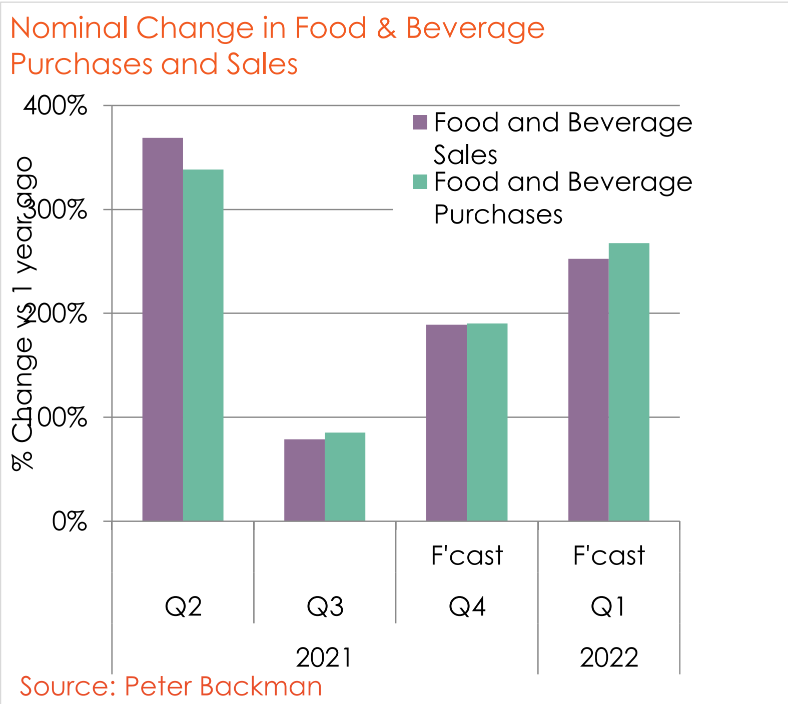
Overall then, this suggests a 40-45% reduction in passenger numbers compared with "normal" 2019 – and this is only slightly down on the post-pandemic peak seen in July (the low point was in April 2020 and there was another dip in February this year).

How much should we read into this? Well, in general it probably provides a reasonably clear picture of travelling to work in London (also bearing in mind that by no means all passenger journeys are work related – there is also travel for shopping and leisure activities, and, of course, an element of travel by foreign visitors is also missing). But how realistic is the reduction of 40-45% for the rest of the country where pressures on working from home may arguably be weaker (because issues arising from the cost and time spent on commuting are less onerous and / or where it may be more important for people to attend their place of work because, perhaps, they are working in a factory)? I suggest that working from home is currently significant and means that, perhaps, only about two thirds of "normal" numbers of people are at their place of work on any single day.

Clearly there are implications in this for feeding at work, and for business at travel hubs and places where workers might spend their lunchtimes.

The implications

Sales, excluding delivery, in the last quarter were running at about 77% of 2019 levels which is a significant on improvement on the 40% in the prior (April to June) quarter. and this accelerated to somewhere closer to 85% during September following the end of the holiday season.



But the pattern is not equally spread across all sectors. Heath care and education were, and still are, running at about, or even above, 2019 levels; in contrast, staff catering was running, substantially below "normal", at about half of 2029 figures,. Hotel foodservice business was 76% of 2019 levels and over three times higher than comparable 2020 figures. The leisure sector showed similar comparable figures.

The rest of the commercial sector continued to gather pace, with sales in the quarter at 80% of 2019 figures and 40% above 2020 sales.

Delivery had been growing at about 20% in the quarter representing a slowdown from the prior period in the face of expanding dine-in business.

For the supply sector, the net result is that the current run rate of foodservice sales is at 78% of 2019 figures, with food growth continuing to outstrip alcohol.

The numbers: The last two quarters – and the next two

The recent past – Q2 and Q3 2021

In this section I summarise the main issues on a sector by sector basis.

However, as I pointed out in my last Quarterly Briefing Report, a significant issue for the supply chain is the changing "shape" of the foodservice sector over the last couple of years. The chart shows the importance of each sector as a purchaser of food in the months at the end of each quarter (Jun = Q2 2021, Sep = Q2 etc). This is a useful guide for suppliers who will want to focus their attention on the sectors which will be showing upcoming importance.

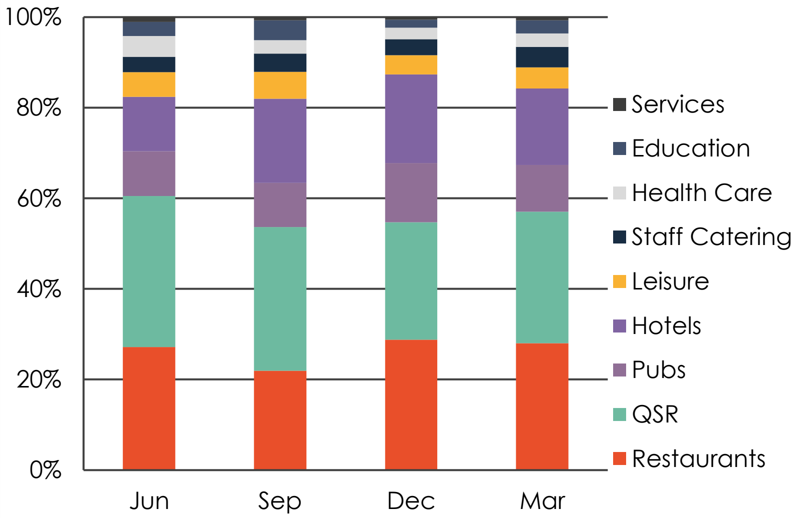
Notable is the evolving importance of the restaurant, QSR and pub sectors

Restaurants, Quick Service and Pubs

The restaurant sector had a small surge early in Q2 as consumers started to dine out after the release on Freedom Day. This surge was overtaken by another surge which resulted from the growth of staycations that I've already commented on.

Mainly as a result of the growth of dine in restaurant meals, the quick service sector gave up some of the gains that had accrued during covid, especially arising out of the growing importance of delivery (plus some welcome growth in takeaway / click & collect business).

"Shape" of foodservice - F&B Sales



Source: Peter Backman

Coffee shops and sandwich bars which catered for city centre lunchtime trade, or which are located in travel hubs and are therefore impacted by heavily reduced local and international travel, saw continuing low levels of demand compared with precovid "normal" levels.

The pub sector has been slower to pick up growth in food sales compared with other "destination" sectors such as restaurants.

Hotels

Travel by air for both holiday and business showed some continuing improvement over the summer but was (and still is) trading significantly below pre-covid levels. Ongoing easing of restrictions on international travel is notable however, and points to continuing growth in this sector, although it is worth noting that Heathrow airport (for example) does not expect to be trading at pre-covid levels until 2026.

This relatively level of international travel clearly had a negative impact on hotel business in London and other metropolitan areas. But, as I have also noted, holidaying Brits made significant use of hotels in popular destinations with bookings at high levels extending into October.

But F&B sales derived from conferences, business meetings, and functions, have been almost non-existent over the past two quarters.

Staff feeding

There has been a recent small, but noticeable increase in working from the office – this is mainly anecdotal but backed up by the figures published by TfL that I've noted above.

This ought to be good news for feeding at work but apart from workplaces that rely on workers being present (primarily manufacturing and some large insurance and other financial institutions), the returning numbers of workers are not sufficiently viable for the operation of full scale catering facilities. These will remain low for quite a while yet.

Health care, education, public services

Over the last couple of quarters, the non-commercial sector (including health care, education, and public services) has broadly been trading at levels close to pre-covid levels. The laggard has been tertiary education and, while this is likely to pick up, it will still remain noticeably below pre-covid levels for the rest of the year and into 2022.

Delivery and dark kitchens

As I've noted, delivery growth has been slowing down but is still expanding. It may be worth noting that aggregators have started ramping up their ultra-fast grocery supply activities. The indications are that they believe this to be more profitable (or at least less loss making) than delivering restaurant meals. If that turns out to be the case, it is likely that their restaurant meal activity will be scaled back with, as yet unknown implications for the restaurant and QSR sectors (and especially those outlets that rely on delivery for a significant share of their sales).

Meanwhile there is ongoing investment in dark kitchens leading to the expansion of delivery capacity. So far, most of this investment is being made in inner London suburbs (and in a handful of other cities – Manchester, Leeds, Birmingham, especially) but the large amount of money that is funding this expansion means that dark kitchens will be set up in other, smaller cities as well. Whether this investment is well placed remains to be seen but for now it will lead to more delivery sales.

The last quarter in conclusion

Here are my headline numbers for the entire foodservice market and its supply chain:

1. Total food and beverage sales in the last quarter – July to August - were £10.8 Billion – almost double the previous quarter

2. Food purchases by operators rose by 50% - below the increases in value of operators' sales

3. Current year on year growth of food and beverage sales is about 80%

The future – Q4 2021 and Q1 2022

The Heatmap

The Heatmap is quite red at the moment – and that indicates difficult conditions. However, the red is concentrated under the heading of "corporate health". The issues described as "Influences on consumer behaviour" are more amber and green. And this suggests that the market will not be too bad over the next two quarters (to the end of March) – but there is a whole set of dangers to corporate health.

In simple terms this forecasts a growing market but one in which individual businesses may show signs of distress and failure. Certainly cash flow is coming under pressure – from rising costs and the need to pay off debt. The budget proposals to reduce business rates for smaller businesses will ease sentiment but the actual impact on cash flow are still for the future,

However taking the positive, all-market view, I feel that we will see reasonable growth over the period. And to underpin that, I am fairly bullish about Christmas trading; this attitude is based mainly on the view that, having had to do without Christmas last year, customers will take the opportunity to celebrate and socialise with friends and business colleagues this year. I have no real evidence for this, but I am hopeful.

So, that is a moderately positive view of the market. But it comes with a caveat that there are no government-mandated restrictions – otherwise known as Plan B - in the offing. If Plan B – more mask wearing, more social distancing, smaller parties – is launched its direct impact on foodservice is likely to be limited. And the indirect, but slightly longer term, impact will be felt through lower covid numbers generally and therefore better conditions for eating out.

I have assumed that inflation – at both cost and sales levels - will be running at 5% by the end of the forecast period in March 2022. This may be optimistic, but I am assuming that, as a result of inflation, operators and customers will be choosing cheaper alternatives. So the effective rate will be less than the headline rate.

I am also assuming that hotel business will start to come back from early 2022 – as global restrictions on travel are eased. But working from home will prove to be very usual and normal, so the return to full scale (precovid) feeding at work will be delayed (and may never return to former levels)

Different sectors – different rates of emergence from covid, and differing growth

My forecasts assume a significant growth in consumer demand at Christmas – benefitting trade in restaurants, pubs, and hotels. But part of this could be put at risk if the sector is not successful in recruiting enough people to operate at most times.

Hotels and leisure are more dependent on both changing consumer behaviour, and for hotels especially, the rate at which international travel returns. And that factor is more dependent on what happens regarding infections in other countries than in the UK.

That leaves workplace feeding which has suffered a loss of business during covid and I believe a considerable proportion of this is likely never to return; and certainly not over the next two quarters. Although this will cause distress for contract caterers, it opens up opportunities for other players – and both Just Eat and Deliveroo have launched services aimed at the eating at work market. I suspect we'll see more activity in this particular area over the next year or so.

Quarterly Trends		2021 Q2	Q3	Q4 F'cast	2022 Q1 F'cast
Food and Beverage Sales					
In the quarter	£ Billion	5.8	10.8	12.6	11.3
MAT (right scale)	£ Billion	19.4	24.1	32.4	40.5
% change vs 1 year ago		369%	79%	189%	252%
Food and Beverage Purchases					
In the quarter	£ Billion	2.2	3.8	4.6	4.2
MAT	£ Billion	7.0	8.7	11.8	14.8
% change vs 1 year ago		338%	85%	190%	268%
Food purchases					
In the quarter	£ Billion	1.7	2.5	2.8	2.6
MAT	£ Billion	5.2	6.3	7.9	9.6
% change vs 1 year ago		293%	77%	139%	175%

Source: Peter Backman

Summary

Highlights of the coming two quarters include:

- Christmas – with the promise (or is it just hope) of a good trading period
- Inflation will work its dark magic and will provide some reasonable growth in nominal – but not real - terms

As always, I produce short term – monthly - data for each market sector, distribution channel, temperature etc. Contact me if you want to access relevant data for your business – to benchmark your existing performance, or to help you assess what your future prospects look like.

Industry news

In my Weekly Briefing Report, I include relevant industry news that relates to the current week. Below I have listed the news items that generally cover a longer time period.

Restaurants

- Benugo turnover fell -72.2% in calendar 2020
- Malhotra Group leisure division sales -79.2% in the year to end March 2021
- Mission Mars sales fell -35.1% in the year to end September 2020
- Giggling Squid net sales fell -11.2% in the year to early April 2021

QSR

- Five Guys UK sales fell -11% in calendar 2020
- Papa John's UK sales rose 29.7% in the calendar 2020
- McDonald's UK sales fell -30.9% in calendar 2020
- Boston Tea Party sales fell -21% in the year to end October 2020

Pubs

- JW Lees sales fell -78% in the year to end March 2021
- Black Sheep Brewery on-trade sales fell -77.2% in the year to end March 2021
- JD Wetherspoon sales fell -38.7% in calendar 2020
- BrewDog sales in its bars division fell -46.5% in calendar 2020
- ETM Group sales fell -78.5% in the year to end February 2021
- Hall & Woodhouse sales fell -38.7% in the year to end January 2021

Hotels

- Center Parcs sales fell -72.5% in the year to end April 2021

Leisure

- Reel cinema sales fell -73.2% in calendar 2020

- DHP Family leisure operator revenues fell -70.1% in calendar year 2020
- Roadchef turnover fell -42.3% in calendar 2020

Suppliers

- Molson Coors sales fell -35.2% in calendar 2020
- Brakspear sales fell -45% in calendar 2020

Around the World

- Bidcorp global sales fell -4.8% (on Rand basis) in the year to end June 2021