

IRELAND'S AGRI-FOOD & DRINKS SECTOR

M&A OUTLOOK DURING AND POST-COVID-19



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The agri-food and beverage sector is Ireland's most important indigenous industry and has seen a surge in export growth in recent years, even against the backdrop of Brexit.

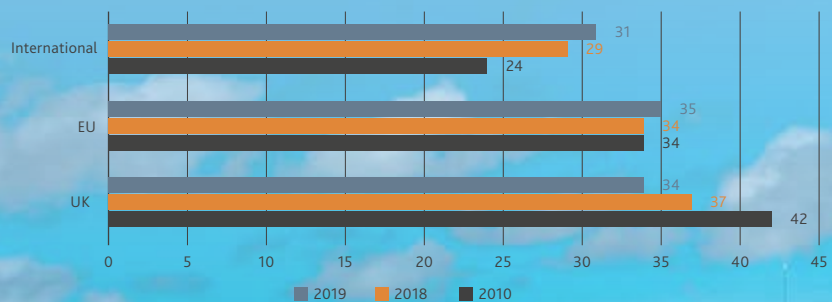
Under normal circumstances, we would be discussing the positive performance of the sector in 2019, with EUR 13bn of exports to overseas markets and a decade of mega-growth where the value of exports in the sector grew by circa 67%.

We intended to highlight that 2020 was likely to be another year of growth, despite the aforementioned Brexit headwinds and the ongoing challenges faced by certain sub-sectors of the industry. With 34% of total exports to the UK in 2019, this was the lowest proportion recorded this decade, reducing (albeit slowly) its dependence on the UK. The EU accounted for 35% of exports, equating to EUR 4.5bn in value, with Irish companies successfully growing their exports internationally to the US, Asia and opening up opportunities in emerging markets as well.

Ireland's drinks industry continues to flourish, with exports increasing by 8% in 2019 with a total value of EUR 1.45bn. There is strong international demand for premium Irish whiskey, craft beer and other liquor products, particularly in North American and throughout Asia.

As a result, we were expecting a high level of transactional activity within the industry, with Irish companies either looking to scale and diversify internationally or in other cases explore how they might secure their current market position in the UK through acquisition. Irish food and drink companies (F&D) have also proven to be attractive targets from both UK and international suitors as they seek to maintain free access to EU markets. The outlook was reasonably healthy for deal making.

However, at the time of writing since the outbreak of COVID-19, things have changed rather dramatically. Societies globally are in lockdown in order to deal with the current pandemic and stem the spread of the virus. As a consequence, world economies have shut down.



COVID-19: IMPACTS SO FAR

The Food & Drinks (F&D) industry has not been spared by the impact of the Coronavirus, with the fallout very different across sectors:

- The Foodservice industry has in effect ceased operations for the time being, with the closure of the hospitality sector;
- A struggling beef industry has been hit hard with the closure of the foodservice sector in Ireland and beyond. For example, the closure of McDonald's restaurants is significant as it is one of the biggest customers of the Irish beef industry, spending more than EUR 160m on Irish beef for its restaurants all over Europe. It has been reported that two out of every 10 burgers sold in its outlets in Europe are made from Irish beef;
- The fishing industry is suffering terribly, both with the disappearance of the foodservice industry and the effective closure of exports markets as demand dries up; and
- For those companies who continue to export, they have experienced a significant increase in shipping costs due to a lack of refrigerated shipping containers internationally. A considerable number of these containers are sitting in Chinese ports.

In short, demand has vanished for certain F&D goods given that countries across the globe remain in lockdown. Most food sectors are trying to adjust to the loss of foodservice sales by pivoting where they can to capture some sales from the significant upswing in retail demand.

There are certain sectors which are benefitting from the current circumstances:

- Some companies involved in non-perishable foods and processed food companies are seeing an increase in sales;
- Moy Park, one of Europe's largest poultry processors, has created hundreds of temporary jobs at its Northern Ireland sites due to increased demand for chicken; and
- There continues to be huge demand for Irish pork in China due to the significant reduction in their national herd following the outbreak of African swine fever in 2018-2019.

In response to the virus, the Irish government recently announced EUR 1bn of financial support measures for COVID-19-impacted companies. F&D companies will look to these supportive measures in part to help them navigate their way through the crisis. However, it's likely more will need to be done to reboot the industry.



WHAT DOES THIS MEAN FOR M&A IN THE SECTOR?

Naturally, COVID-19 has had a profound effect on M&A transactions across all industries, including the F&D sector. We have witnessed a dramatic collapse in activity; with deals stalled, put on hold or cancelled outright. This is on the back of 2019 globally being one of the most active periods for F&D transactions in the recent past.

Overall, it's difficult to predict the full consequences of this global pandemic and when we might emerge from this crisis. With such uncertainty and unpredictability, post crisis the immediate focus of business owners and management teams is likely to be on managing the core business and its recovery. Furthermore, private equity houses are going to have issues within their portfolio companies to manage as well. External M&A is going to be lower down the list of priorities for both corporate and PE firms and consequently M&A activity may be slow to restart.

However, it's our opinion that as we work our way back to the new norm in the aftermath of the Coronavirus, its impact will generate M&A activity. It's difficult to call at this stage what F&D sub-sectors might be involved and what the time horizon might be, but deals are likely to be created out of the following circumstances:

- There will likely be some 'forced M&A transactions' as companies who will not be able to recover from the crisis start to look for buyers;
- Those corporate entities with competitive cost structures, strong balance sheets and cash reserves, along with those PE firms with large pools of cash (despite any portfolio challenges they might have) may seek out cheaper deals. One might expect lower valuations for businesses post-COVID-19;
- There is likely to be consolidation of some companies of a similar size who will seek to combine in an effort to build a business that is able to withstand market uncertainties and strengthen their financial standing by securing new customers/new markets;

- We expect some that M&A activity will be driven by companies looking to remedy supply chain problems. Might we see cash rich retailer groups move into the supply chain through acquisition to procure certainty of supply for some food products?;
- We also expect businesses to seek out value by adding traceability solutions to improve food security. Companies will find themselves facing increasing requirements to satisfy consumers' needs for accurate and transparent information on the food they are producing;
- The virus has had a profound effect on consumer purchasing. F&D businesses will be trying to understand if these changes are permanent and if they need to adjust their businesses accordingly in a post-COVID-19 world;
- When world economies stabilise after the crisis, one might expect the green agenda to emerge more vigorously, with governments and industries demanding sustainable food production processes as the world population continues to grow. Agri-tech companies are leading the way and it's reasonable to expect an increase in M&A activity in this area; and
- Brexit will not have gone away either. As mentioned at the outset of this article, this will create transitional activity in certain parts of the industry, as it seeks to protect itself from the UK's separation from the EU. In addition, UK and international players will continue to look to high-quality Irish food and drink companies, who can provide market access to the EU's 380 million population.

COVID-19 has crushed M&A activity in the short term. However, it will also create new opportunities for those seeking to adapt. Eventually we will ride out this crisis, finding a very different landscape waiting than the one we expected going into 2020. M&A activity will feature for some food and drinks companies in their overall strategy as they seek to rebuild and grow their businesses.

