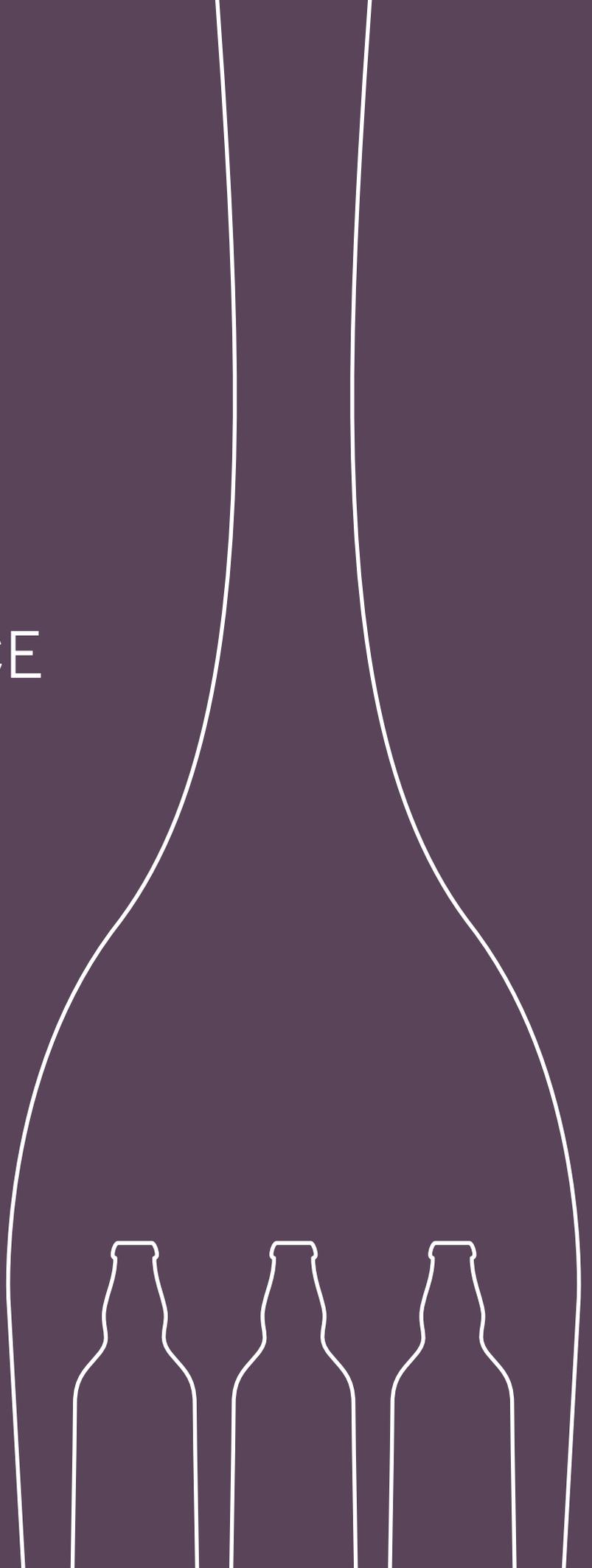


SCOTLAND
OF FOOD & DRINK

INDUSTRY
PERFORMANCE
REVIEW

2018



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SCOTLAND
OF FOOD & DRINK



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INTRODUCTION

Chairman & Chief Executive's view

Past, Present, Future

Scotland Food & Drink (SF&D) is the industry leadership organisation tasked with growing the value of the whole industry and building Scotland's reputation as a Land of Food and Drink

This Industry Performance Review analyses the progress we have made since 2007 when the first strategy, generated by industry and public sector partnership under the leadership of Scotland Food & Drink, commenced. In spring 2017 a new industry strategy, with a vision until 2030, was launched and this report will continue to serve as an ongoing touchstone of our progress.

To gauge past performance, we have used the latest official public data to evaluate historic growth and key performance indicators (KPIs), covering turnover, productivity, research and development (R&D) and exports. Whilst this data is key to tracking our long-term progress its method of collection means it can only take us to 2015 turnover results, or 2016 in the case of exports.

Clearly, given the pace of change in the retail and foodservice markets, the consumer economy and the impending impact of Brexit and other geo-political events, we have included two other measures to provide us with more immediate and actionable understanding. First, our industry partners have given us their own expert insight into the present and future challenges and opportunities within their sectors, using the extensive knowledge and feedback gleaned from their own members and colleagues.

In addition, SF&D has undertaken its third annual Business Barometer Survey, conducted within the industry at the start of 2018. This is designed to look into the near-future and reflect the confidence levels and investment forecasts of businesses, vital indicators in uncertain times.



David Kilshaw
Chairman



James Withers
Chief Executive

Back in 2007, when Scotland Food & Drink was born, industry growth was static. Today, thanks to collaborative working between SF&D and its partners across industry and government, and the talent of producers across the country, our industry is now worth nearly £14bn and growing.

The strength of Scottish brands in the home market has driven real success and with Scotch Whisky and Scottish salmon still the UK's top food and drink exports, we now have a global identity for world class produce.

It is because of this strong platform that we have reset our goals for 2030 and we have outlined a bold ambition of doubling the value of the industry to £30bn.

Achieving 'Ambition 2030' won't be easy. Yet, whilst there are uncertainties facing the industry, not least the implications of Brexit, I believe we have all the ingredients to grasp opportunities and secure success in a rapidly changing world.

I am stepping down from my role as SF&D Chairman after my three-year term, having been Vice Chair for the seven years prior to that. I would like to take this opportunity to personally thank all the businesses, partners, colleagues and forward-thinkers who have been integral to the success of the industry and the SF&D Partnership in recent years. We have collectively achieved something - both in terms of collaborative partnership and industry growth - that was only an aspiration a decade ago. It is now a reality and I know that the continued support from all of you will successfully shape the next chapter in our industry's story.

Food and drink is a national success story and this latest annual performance report highlights the optimism and progress in our sector. In the last ten years, since the formation of Scotland Food & Drink and its unique public and private sector partnership, food exports have more than doubled, sales of Scottish brands in the UK have risen nearly 30% and there is now 120,000 people employed in the sector.

There is much opportunity still ahead of us. Businesses have told us that with even more focus on our home market, we can unlock new growth here and a new UK market strategy is set for launch shortly. In addition, a new national food tourism plan is in development and regional trade events are now creating greater opportunity to link local suppliers with local customers. All this will underpin our international trade growth which continues to set new records.

The SF&D Partnership remains a model for other sectors to follow. Our industry is working collectively and collaboratively and I pay tribute to all the industry associations that work as our partners and are represented through this document. So too, the Scottish Government and its agencies deserve huge credit for supporting a model of industry leadership and aligning their delivery work to the strategy we develop.

So, whether you are on a tractor or fishing boat, on the factory floor or around the boardroom table, I believe this is the industry to be in over the next few years. There will be challenges ahead, from cost pressures to Brexit, but if we deepen collaboration in Scotland even further there is every reason we can make Ambition 2030 a reality and make Scotland a world leader in responsible, profitable growth.

PAST

Industry Progress 2007–2016

Turnover in the Food and Drink Growth Sector stood at £13.5bn in 2015, down from £14.4bn in 2014, a decrease of 6.3% but a rise of 35% from 2007

Since 2007 (the start of the industry strategy) turnover has risen 35%. With over 60% of food and drink sales accounted for by the UK, what happens in this market has a marked effect on the progress of the Scottish industry. In 2015, in the UK, food prices fell by 1.7% in real terms, following a five year period when food prices were rising faster than general inflation. Globally, growth in packaged food revenues slowed markedly; from 2.5% in 2012 down to 1% in 2016. These market conditions have proved challenging for every sector of the Scottish Industry.

Whilst farmers spent less on inputs in 2015-2016 compared to the previous year, there was a bigger decrease in crop and livestock production on average for all farm types. Combined with a reduction in grants and subsidy payments (2015 basic payment), and less favourable market prices, especially for dairy farms, this put pressure on profitability. Income from diversified enterprises rose 19% to average £2,800, with diversified farm businesses achieving average incomes £11,000 higher than non-diversified farms.

Prices in 2015 were also dropping worldwide, particularly milk prices. The average cost for a litre fell from 31.5p to 24.1p between 2014 and 2015, though the volume produced increased 8% to 1.6bn litres.

The average price was to fall further in 2016 to 22.0p per litre, the lowest since 2007, accompanied by a 5% reduction in volume to 1.5bn litres. Consequently, turnover in the dairy sector in Scotland dropped 32% year-on-year.

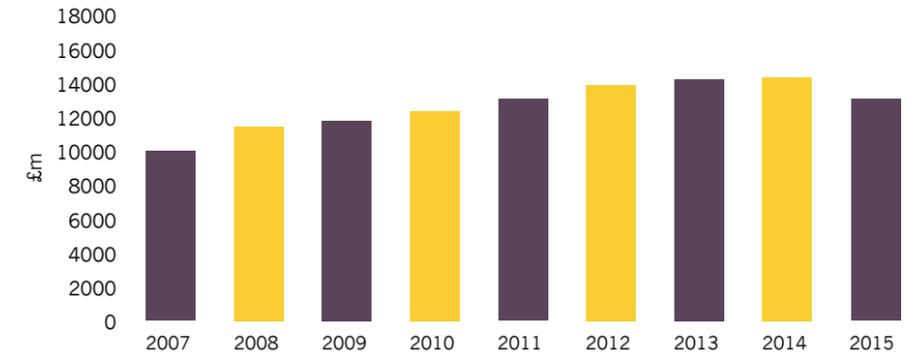
Total sales revenues from the primary red meat processing sector are estimated to have fallen 3% in 2015 to £855m, mainly driven by a fall in wholesale prices. Whilst farmgate cattle prices fell, beef retail prices stabilised, and lamb improved. England and Wales remained the largest market for Scottish processors, generating more than two thirds of all revenues. Export sales rose 11% from 2015, to hit £72m in 2016, contributing to the 91% rise in export value achieved in the last ten years.

Scottish Farmed Salmon total production during 2015 was 171,722 tonnes, the second-highest level of production recorded and capital investment in the industry rose 16% to £63.1m. Exports in 2015 suffered a fall for the first time in five years after the collapse of the Krone made Norwegian fish more competitive, but the situation reversed in 2016 as currency fluctuations boosted exports 17% year-on-year. Around half of all salmon farmed in Scotland is consumed in the UK and, in common with other sectors, deflation in UK retail depressed value sales.

INDUSTRY PROGRESS 2007–2016

Turnover (£m)

KPI Measurement: 2007 to date



Source: Scottish Annual Business Survey 2015 and Economic Report on Scottish Agriculture 2016

Whisky increased in value by £153m to more than £4bn and by volume to the equivalent of more than 1.2bn bottles, an increase of 4% and 4.8% respectively

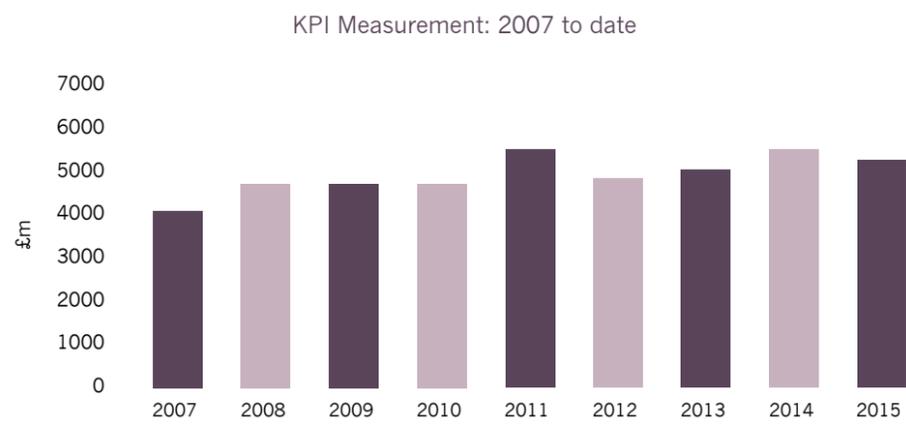
Internationally, 2015 was a tricky year for Scotch Whisky. Exports continued to fall though less rapidly than in 2014. This was largely because of international political and economic developments; stronger sterling in many markets, poor governance and economic decline in others, and the fall in the oil price affecting producer countries. However, in the calendar year 2016, exports of Scotch Whisky increased in value by £153m to more than £4bn and by volume to the equivalent of more than 1.2bn bottles, an increase of 4% and 4.8% respectively.

This is the first time since 2011 that both value and volume of Scotch exports recorded positive annual growth rates, and the first time that Single Malt exports have exceeded £1bn.

Despite the burgeoning numbers of smaller, independent breweries in Scotland turnover in this sector slipped 9% from 2014, suggesting that fierce retail competition from other UK and international brands, downward pressure on prices and a decline in alcohol consumption generally is making for more challenging market conditions.



Gross Value Added



Source: Scottish Annual Business Survey 2015

GVA in the Food and Drink Growth Sector stood at £5.2bn in 2015, down by 2.6% year on year on the consolidated 2014 total but a rise of 27% since 2007

Gross Value Added (GVA) provides a measure for the wealth being generated by the sector and its relative value to Scotland's economy, calculated by the value of the output less the value of inputs used in the production process.

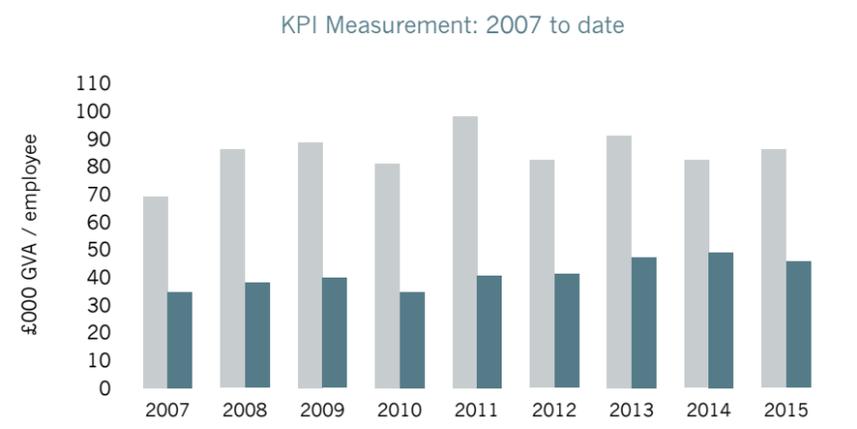
GVA in the Food and Drink Growth Sector stood at £5.2bn in 2015, down by 2.6% year on year on the consolidated 2014 total but a rise of 27% since 2007, equating to £1.1bn p.a. added since the start of the first industry strategy.

Food and drink is Scotland's largest manufacturing sector, accounting for 29% of total manufacturing turnover and generating gross value added to the economy of £3.8bn. This is almost a third of Scotland's total manufacturing value added.

Whilst the high-value nature of drink manufacturing means that it now accounts for 60% of manufacturing GVA, in 2008 this was 66%. This change in balance has evolved as food producers are also developing more premium offerings, with higher output-to-input quotients.



Productivity



Source: ONS Annual Business (Compiled by Scottish Government) 2015

Food and Drink Food only

Food and drink combined has increased its productivity 24% since the start of the industry tracking period

Productivity (measured as £000 GVA / employee) in the food and drink manufacturing sector increased almost 3% from 2014. Whilst the drinks sector started to see a return on its investment in new facilities and state-of-the-art distilleries, gaining almost 10% in productivity year-on-year, food manufacturing lost a little ground, edging back around 6%. However, food and drink combined has increased its productivity 24% since the start of the industry tracking period, in 2007, and food has risen 30%.

In the light of UK and global productivity challenge this should be seen as a strong result; Scotland's food sector

is composed of a large number of smaller businesses that rely on traditional or craft skills to create products of provenance. This usually entails lower levels of technological intensity and thus more modest levels of output per job than can be achieved by the advanced systems of larger manufacturers.

Because the food sector generally has less scope for growth, there is a limit to consumer intake capacity and downward pressure on prices, it has to rely largely on quality improvements. This means that people, skills and innovation are vital to future growth and why they are key pillars of the Ambition 2030 Industry Strategy.



Research & Development Investment



Source: ONS, BERD 2015

The numbers should be considered the tip of a large iceberg made up of a base of widely varying activity

Business Enterprise Research Development (BERD) statistics are produced by the Office of National Statistics to measure investment, by all UK industries (excluding agriculture), in Research and Development (R&D) activity but are particularly designed for research-heavy industries. Whilst the figures are useful to track the general direction of R&D investment in Scotland's food and drink businesses (+40% since 2007) the numbers should be considered the tip of a large iceberg made up of a base of widely varying activity, especially as a significant proportion of research is commissioned by collaborative groups and sector bodies, not captured in the ONS survey.

Examples of this research activity include the microbiological analysis of Scottish fruit juice (to establish the authenticity of single varietal status), generating trained consumer panels to establish a deeper understanding of trout consumption using predictive instrumental sensory analysis, testing of seaweed types for distillation, creating gluten-free beer and developing alternatives to plastic packaging.

Notes on Industry Progress Data

Turnover and GVA is taken from the annual UK-wide Business Survey (Office of National Statistics) with a boosted Scottish sample to improve the robustness of the Scottish data and published as the Scottish Annual Business Survey (SABS).

Figures for agriculture are taken from the Economic Report on Scottish Agriculture 2017.



UK Market



Source: Kantar Worldpanel 2017

In the year to May 2017 retail sales of Scottish food and drink brands in UK were valued at approximately £1.98bn

A combination of supermarket competitive pricing policies and increased spend on retailers' 'Own Labels' continues to impact overall grocery spend. This is reflected in the latest data which shows marginal growth in the retail sales of Scottish brands across the UK market. In the year to May 2017, retail sales of Scottish food and drink brands in UK (based on a representative sample) were valued at approximately £1.98bn, adding around £5m from the previous year and accumulating over £500m extra sales over the decade.

Retail sales of Scottish food and drink brands in Scotland were valued at £585m, down 1% from 2015-16 but up 27% (£125m) from May 2007. As in previous years, retail sales of Scottish food and drink brands in Scotland still account for a larger share (5.6%) of total grocery sales relative to UK (1.8%).

Spirits brands continue to dominate the top ten (by value) Scottish food and drink brands. However, in the year to May 2017, the majority of spirits brands in the top ten saw a fall in retail sales across UK.

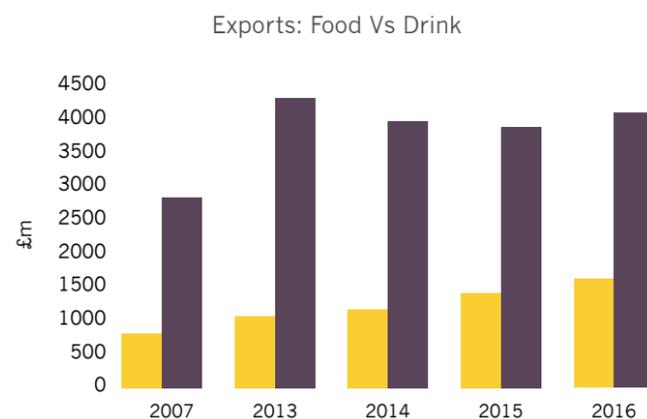
Total spend in the UK Out-of-Home market grew 2% in 2016 to £88bn. With total visits down 2% to 11 billion, diners were spending a little more per visit (source MCA). The number of food-led premises in Scotland (CGA) has increased 16% in the last five years, with a particular growth in cafés, markedly ahead of the rest of the UK. Scotland is also notable for the dominance of independent ownership (around 75% of the market, compared to two thirds in England) and the continued strength of its leased pub sector.



Overseas Exports



Source: HMRC 2017



Source: HMRC 2017

Food Drink

In 2016, overseas food and drink exports from Scotland were valued at £5.4bn, a rise of 6.7% compared to 2015 and a rise of 45% (£1.7bn) from 2007.

Having broken through the £1bn barrier in 2013 food exports from Scotland continue to climb and were valued at £1.4bn, up 13% (£190m) from 2015 and up 111% (£790m) from 2007. The increase in food exports in 2016 was driven largely by a rise in the value of exports to Europe (£177m), Asia (£47m) and North America (£21m).

The fish and seafood category recorded the largest overall increase, up £156m (26%), with Europe leading the increase (£133m). Whilst Scottish Farmed Salmon remained Scotland's largest single food export (£444m in 2016) trade fell in a number of key markets, largely due to currency fluctuations, particularly the lower level of the Norwegian Krone. However, initial figures released by HMRC for 2017 show a significant increase in overseas trade with value up 35% to £600m and volume increasing 26% compared to 2016. The United States remains the largest market for Scottish salmon, followed by France, China and the Republic of Ireland.

In the calendar year 2016, exports of Scotch Whisky increased in value by £153m to more than £4bn and by volume to the equivalent of more than 1.2bn bottles - an increase of 4% and 4.8% respectively. This is the first time since 2011 that both value and volume of Scotch exports recorded positive annual growth rates, and the first time ever that Single Malt exports have exceeded £1bn. But bottled Blended Scotch Whisky is still by far the biggest category. It accounted for 69% of all Scotch volumes and values exported in 2016.

Scotch Whisky was directly exported to 182 countries in 2016, up from 174 in 2015. Indirectly, due to re-distribution hubs, Scotch is likely to reach more than 200 countries and approximately 80% of Scotch exports by volume and value are supplied to the top 25 markets. Single Malt Scotch Whisky was the stand-out performer in category terms during 2016. More than 113m bottles of Single Malt were exported and the valuation surpassed £1bn for the first time.

Red meat exports climbed 11% in 2016 £72m, of which 90% was to Europe. Exports to Germany increased by 23% and to the Nordic countries, Poland, the Baltic states, and other central and eastern European countries they rose by 19%, 197% and 444%, respectively. The key markets for Scotch Beef and Scotch Lamb were France and the Benelux nations.

PRESENT

A view from the sectors



Scotch Whisky Association



Karen Betts
Chief Executive

Scotch Whisky accounts for a fifth of the UK's food and drink exports, supporting more than 40,000 jobs across the UK

Record-breaking export figures for 2017 underpinned Scotch Whisky's pre-eminent place in the global marketplace and its importance to both the Scottish and UK economies.

Scotch Whisky accounts for a fifth of the UK's food and drink exports, supporting more than 40,000 jobs across the UK – 7,000 of which are in rural areas of Scotland. We expect to see further growth in 2018 and are working closely with our partners and Scottish and UK Governments to create the conditions for continued success at home and in overseas markets.

Despite the uncertainty caused by Brexit, the export value of Scotch rose to a new high of £4.359bn last year, topping the previous high of £4.273bn in 2012. Every second 39 bottles were shipped overseas in 2017 and these exports earned our country £139 every second. The USA, traditionally our largest market by value, grew by 7.7% in value over this period and 7.4% in volume. Emerging markets, such as India which grew 14% last year, continue to represent enormous opportunities.

As some 20m casks lie maturing in warehouses in Scotland, it's very important to the industry that our global markets remain robust and resilient as the UK navigates Brexit and establishes new trading relationships around the world. We have undoubtedly benefited from recent falls in the value of the pound, as have other exporters. But this short-term boost will not distract the industry from working hard to secure the conditions for long-term growth.

With nearly a third of Scotch Whisky exports being shipped to the EU, it's vital that the UK Government secures as smooth trade conditions as possible, alongside pursuing ambitious free trade deals with key markets around the world, tackling trade barriers and making Scotch more competitive on the international stage. We will continue to work to secure robust legal protection for Scotch at home and abroad as we look to form closer ties and trading relationships post Brexit.

Confidence in the future is reflected in high levels of investment in the Scotch Whisky industry. There has been a 19% increase in distilleries since 2013, with the new Isle of Raasay Distillery and Clydeside Distillery in Glasgow being joined by the Macallan distillery and visitor centre.

Whisky is not only one of Scotland's most valuable exports, it is also becoming a valuable draw for tourists interested in learning about the heritage of our national drink. In 2016, we welcomed a record 1.7m people to over 40 Whisky Distillery Visitor Centres across Scotland, with one in five tourists visiting a Whisky Distillery during their stay, each spending £31 per visit. The increasing number of Whisky tourists is a boon for the wider Scottish economy as hotels, pubs and restaurants reap the benefits of the increased investment in customer experience by Whisky distillers.

So, let's raise a dram to one of Scotland's most strategically important, historic and popular international exports.

Seafood Scotland



Iain MacSween
Chairman

We now have a once in a lifetime opportunity to ensure the seafood sector can face the challenges of the future with a viable and sustainable industry

Change and uncertainty are two of the staples of the fishing industry and some of the recent changes have clearly been beneficial as far as the industry is concerned.

The recent decision to award MSC accreditation to North Sea cod is the successful conclusion of a process that witnessed the cod stocks recover from historically low levels to a level that is now sustainable moving into the future. With other major stocks in a similar position there is hopefully no reason why the industry should not continue to develop innovative new products, find new markets at home and abroad whilst expanding existing markets, thereby continuing the contribution the seafood sector makes to the economy in general.

But there is no doubt that whilst the industry is in a relatively good place at the moment, it faces a period of great uncertainty. This is, of course, due to Brexit.

On the day the UK leaves the EU, we will become a coastal state. The constraints of the Common Fisheries Policy will no longer apply to the industry. Or will they? Despite the oft asserted mantra by commission spokespersons that there can be no cherry picking, we have the President of the EU stating that EU vessels should retain access to British waters. They want continued access to our waters to retain in place a policy framework that has acted against domestic catchers and processors since it was introduced and there is the on-going threat that a loss of access will result in a loss of market access.

Iceland and Norway grant no access in return for market access that is the norm in fisheries agreements. Why should the UK depart from that principle? Perhaps they need to be reminded if the produce that flows into the UK from other parts of the EU's agricultural sector. We now have a once in a lifetime opportunity to ensure the seafood sector can face the challenges of the future with a viable and sustainable industry based on the vital natural resources that are around our coast. Why should we let that opportunity pass us by?

Scottish Salmon Producers' Organisation



Scott Landsburgh
Chief Executive

Our biggest success in the last year was increasing our exports 35% in value and consolidating our position as the UK's biggest food export

Our biggest success in the last year was increasing our exports 35% in value from the previous year and in doing so, consolidating our position as the UK's biggest food export with overseas sales of some £600m in 2017. This is a sign of an industry in good health. Additionally, our latest economic report illustrated the continuing success of the industry in terms of increased employment, participation in training schemes, capital investment and wage growth, particularly in some of Scotland's most remote areas.

The industry faces continued environmental challenges. People talk about climate change and it can often be quite abstract. But in recent years, rising water temperatures have conspired to make the environment we operate in significantly more challenging. Most, if not all, the environmental issues we have had to deal with are a result of changes to the marine environment over which we have little control.

There are two priorities for the year ahead. First, Brexit. We need to work with our stakeholders in advising and influencing the negotiating parties to understand and reflect our many concerns about a new, international trading environment. A trading environment in which our short shelf life, perishable product must travel from the harvest station and across borders to dinner plates as quickly as possible. There are several other Brexit-related issues, but this is the crucial one and we must keep pressing those negotiating for an outcome which continues to allow this to happen with the minimum of friction and cost.

Second, getting our political engagement right so that the public understand how we are delivering for the economy whilst working exceptionally hard to overcome our environmental challenges. Through our involvement in the Industry Leadership Group and in the new Strategic Framework for Farmed Fish Health, we will demonstrate our work on these fronts. We seek sustainable growth and this type of engagement is critical to that aim.

Collaboration is undoubtedly working but we need to do more. Across the food and drink sector, of course, but also between our domestic salmon industry and our international competitors, between ourselves as salmon producers and Government and more generally and broadly with all industry stakeholders.

Our work with our counterparts in other food and drink sectors has given us a greater voice and the dissemination of knowledge and best practice has been invaluable to my organisation and our industry throughout the last year. Understanding how other sectors cope with challenges and how they try to grow despite them offers fantastic insights. Likewise, I hope the sharing of our knowledge and experience provides the same value for others in the food and drink sector.

Quality Meat Scotland



Alan Clarke
Chief Executive

Our economics services work ensures businesses in the Scottish red meat industry benefit from the latest statistics and analysis

Our biggest success has been delivering strongly for our levy-payers and playing a lead role in building on the world-class reputation Scotland has for its high-quality food. Our activities have included promoting the industry's brands, Scotch Beef PGI, Scotch Lamb PGI and Specially Selected Pork, in Scotland, the wider UK and international markets.

Our industry development work focused on improving the efficiency, profitability and sustainability of farmers and others in the red meat chain in Scotland and our quality assurance schemes saw around 10,000 members benefit from the consumer confidence they deliver. Our health and education work focused on the importance of a healthy diet and red meat's role in achieving that. Our economics services work ensures businesses in the Scottish red meat industry benefit from the latest statistics and analysis.

The biggest challenge for the red meat sector is the prevailing uncertainty around Brexit. During the past year, QMS has continued to inform the discussion on the future shape of the industry, including the production of a series of briefing papers dealing with the key Brexit challenges as we see them.

Access to markets is a priority and it has been encouraging to see that the importance of non-UK workers is being recognised particularly in the food production and processing sectors. The future shape of agricultural support remains unclear as does the position regarding the European grants for product promotion which QMS has previously worked hard to secure.

We have all the ingredients for success; globally acclaimed red meat brands which are underpinned by robust quality assurance and produced in a sustainable manner that makes animal welfare a priority. We also have a unique asset in the people who work in our industry. Their skills, passion and commitment are invaluable.

At the start of 2018 we undertook a review of our strategy and identified the key areas that we need to tackle in the future through effective collaboration with the businesses and organisations in our footprint. The delivery of activities that support this strategy is our top priority for the year ahead. Our strategy is "to support the sustainable, professional and resilient development of a profitable Scottish red meat industry".

We have identified four strategic aims supported by strategic objectives which will guide our implementation plans and our future activities. These include: building our brands; supporting sustainable growth; developing capability and capacity within the sector and delivering a range of professional services to assist the industry to achieve its aims.

The Scotland Food & Drink collaborative model has brought us many benefits, including working in partnership with the wider food and drink industry to shape Ambition 2030. Our new strategy is aligned with Ambition 2030 and we believe that a collaborative approach is essential to achieve an effective and efficient red meat supply chain in Scotland.

Scottish Bakers



Alasdair Smith
Chief Executive

Developing the skills of the next generation continues to be an important challenge for the sector

It is my great privilege and honour to have been appointed Chief Executive of Scottish Bakers and National Food and Drink Training in January 2018, and I am grateful to the President, Craig McPhie, and his board, for putting their faith in me to fill this crucial post.

The Scottish Bakery sector continues to play an important part not only across the Scottish economy, but also in the communities where many of these businesses operate. From small, independent High Street bakers to large process manufacturers, the sector continues to thrive; providing employment, creating value and producing magical products from the humblest of ingredients.

Developing the skills of the next generation continues to be an important challenge for the sector, and Scottish Bakers is proud to play an active part, though National Food and Drink Training, in supporting nearly 450 Modern Apprenticeship starts last year. With valuable support from Skills Development Scotland, we provide training across 11 different MA pathways including traditional craft bakery skills as well as broader food manufacturing operations roles.

However, the year has not been free from challenges. Dairy prices, for example, an essential ingredient for most bakers, have risen dramatically; trebling at one point before falling back slightly. Such dramatic price fluctuations squeeze margins, and therefore limit bakers' abilities to invest in other areas of their operations; from skills and new product development, to plant and machinery.

Regulation and the impact of policy to tackle public health issues also affect the sector. Manufacturers are looking for ways to maintain the integrity of their leading products while working with legislators and health experts to reduce sugar and fat content.

And of course, the exit from the European Union is playing hard on some manufacturers minds, especially those who depend on workers from other parts of the EU. We will need to be mindful in this coming year of potential increases in demand for training and recruitment to replace skills lost if migrant workers choose to return to their homelands.

Scottish Bakers is firmly focussed on ensuring capacity to train the next generation is in place. With demanding targets for recruitment of apprentices, we are committed to modernising our own processes to move towards digital capability for assessment and recording of evidence. We believe this will bring added flexibility to our training offer, ultimately helping to drive productivity, quality and ambition in the sector. None of what we do could be achieved without widespread partnership and collaboration with the public and private sector stakeholders.

But the greatest acknowledgement must go to those members of Scottish Bakers who represent our tradition, our history and our future. Without an active membership and trade association, the sector would be a poorer place and we look forward to continuing this journey together for many more years to come.

National Farmers' Union Scotland



Scott Walker
Chief Executive

Farmers and crofters are not yet feeling that the success being enjoyed elsewhere in the chain is benefiting them

What has the past year felt like to the farmers and crofters of Scotland? According to official income estimates average incomes have risen. So maybe the industry is at last benefiting from the growth and success of the Scottish food and drink industry. Perhaps supply chains now see the need to pay a fair share back to the primary producer to secure product and to provide the profitability needed to invest and secure future supplies. Perhaps the success of the industry, built on strong Scottish providence, is now rewarding the start of the chain; the farmer and the crofter on which this providence is built. This is what I would like to be able to say. I would like to be able to say that farmers are feeling part of the successful Scottish food and drink industry. But the reality is somewhat different.

As is often the case you have to look behind the headline figures. To put the figures into perspective they are still down 46% in real terms since 2011/2012. And if you dig just a little deeper you find that 45% of farms are not able to pay the farmer, spouse and other working family members a rate of pay equal to the minimum agricultural wage. Farmers and crofters are not yet feeling part of a successful supply chain. Farmers and crofters are not yet feeling that the success being enjoyed elsewhere in the chain is benefiting them. For many, just surviving remains difficult.

We have the ambition to double the size of the food and drink sector in Scotland by 2030 but if all are to benefit from this we will need to radically rethink how the supply chain operates. Farmers, crofters and their families want to feel valued partners in the supply chain, they need a fair sustainable price if we are to maintain and hopefully increase the output from our farms.

I have said before that working together sometimes requires a leap of faith. To get the supply chain to work will require all sides to put aside their distrust of one another. We can achieve so much more if the supply chain were to work together with one collective goal. Innovative ways of working are possible. Scotland Food & Drink has been successful in bringing the Scottish industry closer together. Now we face our biggest challenge and I look forward to continuing to work to solve the biggest challenge of them all; delivering a successful supply chain. It has often been said that if something is easy it's not worth it. Well, building successful supply chains that deliver for all certainly is not easy, but it will be worth it when we deliver it.

Scottish Dairy Growth Board



Paul Grant
Chair

The year ahead is about introducing increased processing capability and building sustained growth in recently opened markets, USA, France, Japan and Canada

It has been a year of encouraging progress and, as a result, the initial three-year funding programme was extended for a further year, with the likelihood of a further two-year extension. The successes of the year were based on three key areas of activity. Firstly international; first orders going to two new markets, France and Japan. Also, the Canadian Importation Quota is being lifted for early 2018 so we start business with a leading importer, secured in 2017.

Second, two further significant processing projects are receiving major grant offers, one is already operational, the other should start up in 2018. A previously approved project remains possible and again could start up in 2018.

Third the Dairy Hub, which has further developed its positive reputation, responding to over 50% more enquiries than the previous year.

There were as always challenges, the most significant being the tightening of importation requirements driven by the major retailers in those overseas markets. BRC accrediting is becoming the standard for volume, branded opportunities.

The year ahead is about introducing increased processing capability and building sustained growth in recently opened markets, USA, France, Japan and Canada. We also plan to start trading in Germany and Scandinavia this year.

This Growth project requires all associated partners to work transparently and collaboratively to succeed. The resources of the Scottish Government, SDI and the in-market team and Roddy Wilde, the sector coordinator, have been key and will be essential going forward.

Food and Drink Federation Scotland



David Thomson
Chief Executive

The top priority for the year will be making sense of Brexit and ensuring that our food and drink industry continues to thrive

The biggest success of the year has to be the launch of Make Innovation Happen. Innovation is important to the future growth and success of the whole food and drink industry. The Scotland Food & Drink Partnership, Scottish Enterprise and Highlands & Islands Enterprise launched this service which connects Scottish businesses with a range of support from public sector and academia. It is great to see companies making use of this service and partners coming together to make it easier for businesses to navigate the support that is available.

The challenge in the last year has to be toss-up between Brexit and health! The uncertainty of Brexit affects everything including workforce, exports and law. We have engaged with Scottish and UK Governments and politicians of all stripes to ensure food and drink is at the top of their minds. And the health agenda is a challenge for all of us.

Obesity needs to be tackled and industry needs to play its part but what is the best way of doing that? We have responded to the Scottish Government's Diet and Obesity Strategy consultation and will continue to work with Government, Food Standards Scotland and industry partners to help make a real difference to Scotland's health.

The top priority for the year will be making sense of Brexit and ensuring that our food and drink industry continues to thrive. At FDF Scotland we are determined to secure the best outcome for Scottish and British food and drink businesses and their consumers.

Collaboration is definitely working. Scotland's food and drink industry's success has been supported by the collaboration that the Scotland Food & Drink Partnership has fostered over the last decade. We are much stronger working together and as our country's future develops we need to stick together to deal with the challenges that will, undoubtedly, come our way.

Fruit, Vegetable and Potatoes Industry Leadership Group



Allan Bowie
Chair

Increased awareness for healthy foods both here and abroad will provide incentives in this sector to build extra capacity to meet demand

The Industry Leadership Group (ILG) in fruit, vegetables and potatoes (FVP) has been setup by the Scotland Food & Drink Partnership, supported by Peas Please, to develop a sector action plan for the industry led by the industry.

Scotland currently grows a third of the UK's soft fruit (£134m), nearly a quarter of the UK's potatoes (£215m) and has greatly increased vegetable production over the last decade (£155m in 2017). The total value from the FVP sectors is about 17% of Scottish farm output. The UK is currently 40% self-sufficient in production of fruit & veg and highly reliant on imports to satisfy consumer demand, with trends in domestic production and value continuing to rise, alongside increased competition.

Adoption of new technologies/innovations, strong capital investment, often in producer organisations, and a mindset to harness new skills has driven growth and value within the sector will only help increase our self-sufficiency.

Increased awareness for healthy foods both here and abroad will provide incentives in this sector to build extra capacity to meet demand. Increasing consumption of FVP and its links to a healthier nation must be at the heart of any future strategy.

Strong collaboration, innovation, research and development and strong market messages within the supply chain will make this happen.

This sector has voiced very strong concerns about the availability of EU labour and market access after Brexit clear decisions will need to be made this year to address these fundamental and important issues. These people work extremely hard, are highly valued within the supply chain and are essential to the proper functioning of this sector and the wider economy.

The ILG will be looking at marketing, innovation, the supply chain and people skills as strategy themes, in addition to the added health benefits and reduction of waste that society is expecting from this sector. Competitiveness and market growth will be very important but maintaining the skill set and drive of the people in the industry will be key to achieving Ambition 2030.

I know there is a strong competitive and collaborative will within the sector to meet head on these challenges and a can-do attitude to deliver the benefits. I am looking forward to working with all to deliver this vision.

Scottish Agricultural Organisation Society



James Graham
Chief Executive

Our efforts remain as determined as ever, building on the established co-operative business sector that turns over about £2bn per annum

One of the most important statements made by Scotland Food & Drink is "everything good that has happened in achieving our goals, has happened because of collaboration." Building on the experience and evidence of the last few years, Ambition 2030 adopted a growth strategy that positions supply chain collaboration as a top priority in delivering stretching targets for further growth.

The evidence is clear cut that when all supply chain partners collaborate in responding to market signals and forecasts, and to market changes, they discover efficiencies, optimal performance, and confidence in investment decisions at each point in the chain.

The initial three years of the Market Driven Supply Chain programme that we implemented on behalf of Scottish Enterprise concluded in the spring of 2017. It facilitated fifteen UK projects and seventeen export projects, resulting in an estimated £61m of additional sales over three years, with potential of a further £85m in sales and efficiency gains. All the projects involved at least two 'links' in the supply chain collaborating, and often more. The programme was renewed for a further three years and our intention is that the scale of impact becomes ever greater, as the economic gains of collaboration really take hold.

Collaboration amongst farmers is now usually a pre-requisite for collaboration in supply chains, aggregating farm output into meaningful volumes of consistent quality produce. Our efforts remain as determined as ever, building on the established co-operative business sector that turns over about £2bn per annum and is vitally important across much of the industry. We have indicated to government our proposals for future policies that would positively encourage farmer co-operation on the basis that to do so will realise significant economic gains for farmers, and strengthen their competitiveness in supply chains, as well as strengthen Scotland's food and drink industry.

The feasibility of fully utilising data technologies through the entire chain for the benefit of all in the chain, to inform decision making is stronger than ever, but as yet, remains at an early stage of adoption. Now is the time to be innovative in supply chains and start creating new business models and processes making the best of all Scotland's potential. And there-in lies the means to achieving the 2030 vision: "supply chain relationships are transformed. Farming and fishing businesses, manufacturers and buyers view each other as partners; collectively they drive profitable and more equitable growth in markets both new and long-established".

Scottish Craft Distillers' Association



Alan Wolstenholme
Chair

Our organisation is still in its infancy and our sector is realising that a strong, united voice is necessary to achieve the growth we desire

The Scottish craft distilling sector is booming and new distilleries are rapidly opening across the country. In order to continue supporting our members and the sectors growth, we have joined forces with Scotland Food & Drink (SF&D). This is our biggest success of the last year. Our new alliance will help the Scottish Craft Distillers Association (SCDA) to reach a new level of operation, leaving its 'club' origins behind and supporting us to build stronger relationships with the industry, other key trade bodies, in particular the Scotch Whisky Association and the Scottish Government and its agencies.

Protecting our provenance story remains to be a challenge for the sector. We have faced similar issues to other sectors where the market opportunity emerges faster than the domestic production capacity. In an age where authenticity and provenance are held in such high esteem by an increasingly inquisitive consumer base, ambiguous claims about origin are being examined more closely and consumers deserve to know that when they buy a craft spirit with a Scottish place name on the label, that the spirit is distilled and bottled in Scotland.

In order for us to provide this reassurance to the consumer, we have created a strict set of criteria which a business must meet to be part of the association and to receive the SCDA accreditation; distillers must own and operate a still as well as manufacture and bottle in Scotland. In addition to this, survival and enduring growing pains for the organisation will be a real challenge, as will the problems which come with success for our members who often struggle to access distribution chains for expanding product volumes and who are starting to export overseas.

Our members work well together by cross-promoting and sharing best practice. Our organisation is still in its infancy and our sector is realising that a strong, united voice is necessary to achieve the growth we desire. Our key goal is to grow the Scottish distilling sector, protect the authenticity of Scottish craft spirits, and help distillers achieve their goals. By working with SF&D, our members and the whole supply chain, we can not only achieve this, but we can prove that the SCDA is here to stay.

The Brewers' Association of Scotland



Scott Williams
Chief Executive

With success comes challenges as the sector finds increased competition in the home market as the number of new entrants rises

It has been a great year for The Brewers' Association of Scotland (TBAS) and our biggest success has been the growth of our membership base.

The large number of Scottish brewers who have chosen to join the organisation and engage with us has given us greater visibility and credibility as well as adding fresh ideas and perspectives. This new outlook also allows us to work in a more holistic manner which benefits all our members and the industry.

The Scottish food and drink story is a real success and the beer revolution is at the heart of it. But with this success comes challenges as the sector finds increased competition in the home market as the number of new entrants rises.

It is fair to say that the sector has grown at a slower pace than the added capacity brought by new Scottish brewers which makes the focus on creating new market opportunities across the globe for our brewers a key priority.

In addition to creating new opportunities to benefit the brewing sector, our key priority as an organisation is ensuring the growth of our membership and delivering real results for our members.

All of this work demonstrates that collaboration in our sector is working. The Scottish brewing sector is a community and we all help each other out where possible. This can be as simple as offering to loan ingredients in emergencies to assisting with debt recovery and advice on paperwork. Overall, I am optimistic about the year ahead both for the organisation and for the brewing sector.

Scottish Environment, Food and Agriculture Research Institutes (SEFARI)



Prof. Colin Campbell
Chairman

In Scotland we have ready access to world-leading research expertise, underpinned by Scottish Government funding. Many growers, producers, farmers and food industry practitioners will be aware of the work of Scottish Institutes such as Scotland's Rural College (SRUC), the James Hutton Institute, and the Moredun Research Institute. The last year has seen the emergence of SEFARI (Scottish Environment, Food and Agriculture Research Institutes) as a new collective comprising SRUC, Hutton and Moredun, with the Rowett Institute at the University of Aberdeen, Biomathematics and Statistics Scotland and the Royal Botanic Garden Edinburgh. Each brings world class expertise, relevant to the Ambition 2030 strategy, the Good Food Nation agenda, and associated cross-cutting issues of climate change, healthier food choices, food security, biodiversity, and rural economy.

Longer-term strategic research is fundamental but must also deliver to those with short-term needs; a farmer making a land use decision, a business deciding how to invest, an individual making food choices, or a policymaker looking for a new solution. Collaboration between SEFARI, industry and policymakers is vital for this innovation agenda. In 2016-2017 SEFARI was engaged in 356 external collaborative projects, over half of which involved international partners.

Our Scottish Government funded SEFARI research contributed £151.8m GVA to the Scottish economy in 2016 and supported around 1,460 jobs. We work daily on innovative research through the food chain, whether exploring new food and drink crops, making livestock and arable agricultural systems more efficient, or rethinking how we turn waste into resource. An example of the latter is using vegetable and fruit waste differently to substitute for synthetic chemical antioxidants, increasing supply chain profitability.

SEFARI is part of the Make Innovation Happen programme, helping food and drink businesses stay a step ahead, and we help deliver the Rural Innovation Support Service, designed to innovate from the bottom up, helping rural businesses stay competitive.

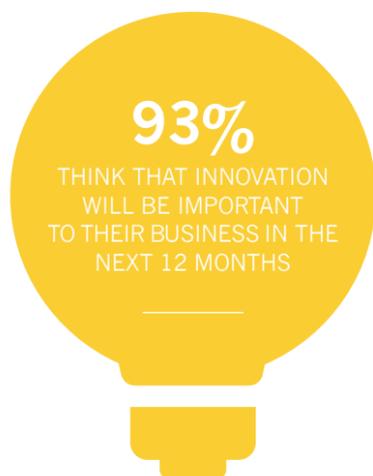
SEFARI is working with Scotland Food & Drink, the Scottish Government's Agriculture Champions, the Leadership Group on Fruit, Vegetables and Potatoes, and is well represented on the Scottish Food Commission. Through the SEFARI Fellowship programme we are working with Food Standards Scotland on what information is required to profile Scotland's food industry, and map food supply chains, vital at a time of geopolitical uncertainty. We will deliver more in this space over the next year, linking research to the needs of business and policy, and delivering leading ideas for better lives.

FUTURE

2018–2019 Outlook & Business Barometer



2018–2019 Outlook



Global food commodity prices are projected to remain low over the next decade compared to previous peaks, as demand growth in a number of emerging economies is expected to slow down and biofuel policies have a diminished impact on markets, according to the latest 10-year agricultural outlook published by the OECD and FAO.

World economy growth is expected to remain relatively stable in 2018, just above 3%. Brexit is expected to have a major negative effect on growth in the UK, which is projected to drop to below 1% for 2018-19. Despite the robust growth projections for Germany and France, Brexit, and the much slower growth in the main Mediterranean economies, are expected to result in lower economic growth in the EU in 2018.

Cyclical problems such as currency fluctuations, a slowdown in emerging markets and the difficulty of raising prices because of low inflation in the US and much of Europe, have all contributed to making the consumer environment in 2018 one of the most uncertain in 25 years. In Scotland, business surveys signal that business optimism, on balance, improved over 2017 but remains moderate. Scottish consumer sentiment weakened in Q4 2017, but the security of household finances is expected to improve over 2018.

In UK multiple retail, private-label products are expected to continue their strong growth, fuelling the development of retail discounters and extending the price war between

supermarkets and online sites, including the increasingly influential Amazon. Brands will have to ensure their products are superior to justify the price and they are likely to achieve this through showcasing heritage and new products.

As shoppers continue to value innovations that offer convenience and time-saving solutions retailers will increasingly use artificial intelligence to analyse customer information to predict and fulfil shopper demand using automated delivery. Health and wellness will continue to be a focus throughout 2018 and retailers are expected to expand designated zones in-store and develop lifestyle-focused formats.

The overall UK eating out market is forecast to enjoy positive value growth in 2018, with a modest rise of just 1-2% the most common expectation. However, price inflation is likely to be above 3%, indicating the high likelihood of negative underlying volume growth.

Delivery players, contemporary fast food and food-to-go are the segments expected to perform best. All these channels align well with the growing trends towards more adventurous, informal and healthier, eating, whilst benefitting from strong value-for-money credentials. Analysts expect craft beers and spirits to continue their rise in on-trade, both in the UK and developed markets overseas, and there will be more opportunities to increase sales in soft drinks, especially low-sugar options, in UK foodservice.

Business Barometer Survey 2018



Survey Details

January 2018 saw the third annual Business Barometer Survey, conducted specifically for this report, which aims to assess the level of confidence for the next twelve months in Scotland's food and drink businesses. Alongside the regular questions on the economic climate, anticipated investment in innovation and exports this is the second year we have also asked businesses to forecast how Brexit might affect their own companies and the wider industry.

Survey Output Summary

Our respondents' confidence in the general economic climate in the UK for 2018 was almost exactly as it was for 2017, right in the middle of the scale that runs from pessimism to optimism. Their views on the global economic situation were also very similar to last year, being slightly more positive about the world outlook.

The same can't be said of views on the likely effects of Brexit on businesses where opinion has hardened; 82% think the decision to leave the EU will have negative consequences for their business, up from 48% in 2016, with most of the shift coming from those who stated they "didn't know" last year. The same pattern is reflected with regards to the consequences for Scotland's food and drink industry as a whole where three quarters of respondents think it will have negative effects.

Despite this, over half of companies are positive about their own prospects, forecasting turnover increases of more than 10% across 2018-19. Some of the biggest changes in respondents' views came in answer to the

question on factors that would could limit business growth. Whereas in 2016 and 2017 17% thought that an absence of skilled labour was likely to inhibit their ambitions, this has leapt to 40% in 2018, reflecting other industry surveys and forecasts. Despite this the number of companies expecting to increase overall staff numbers has risen 24%. Concerns about the cost of inputs, currency fluctuations and access to finance have also heightened markedly in the last year.

Turning to the importance of markets, those reporting that the UK will be more important this year has almost doubled and nobody thinks it will be less important. This hasn't diminished the role of exports with those believing that they will become more important at 62%, the same as both 2017 and 2016.

A more focused attention in non-EU markets for exports is very apparent from the 2018 survey; Greater China, Japan and North America all show a near doubling in interest. Importance of innovation has risen from 78% to 92% and there are two standout areas where companies believe they'll be investing; new product development (93% of businesses) and packaging, 68%. Alongside innovation sits industry collaboration and 82% believed this was important for industry development, more than half thinking it "very important."

Since 2016 one question has scored consistently high on the "important" or "very important" metrics; Scotland's global reputation as a 'Land of Food and Drink' has carded over 95% for each of the three years.

Survey conducted online, January 2018
Total Company Sample 48

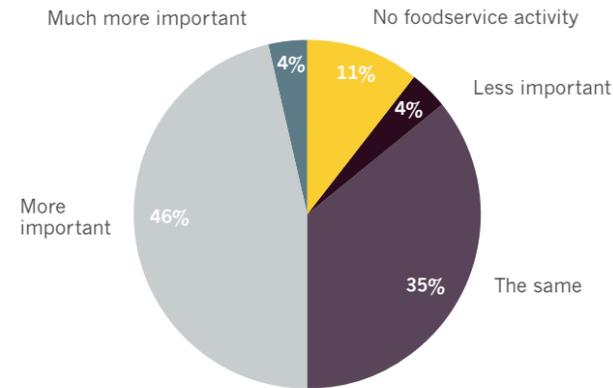
Do you think the UK's intention to leave the EU will be positive, negative, or have no effect on your business?

82%
NEGATIVE

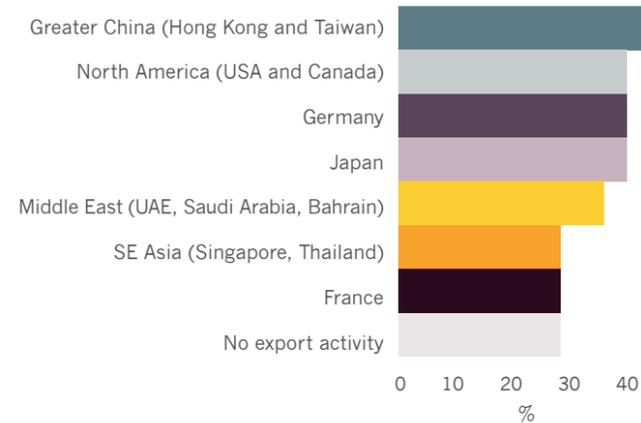
Will you invest more, less, or the same in innovation in the next 12 months?

68%
INVEST MORE

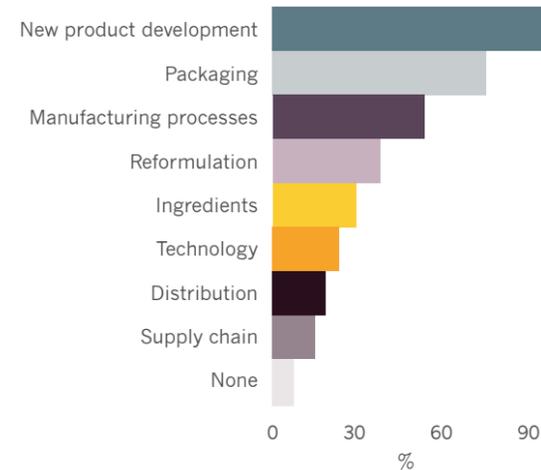
How much more important will the UK foodservice channel be to your business in the next 12 months?



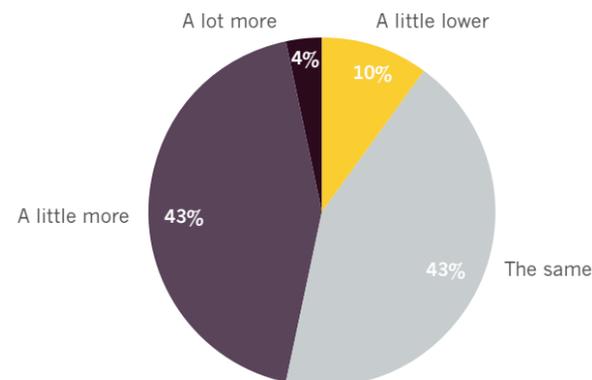
Which export markets will you target in the next 12 months?



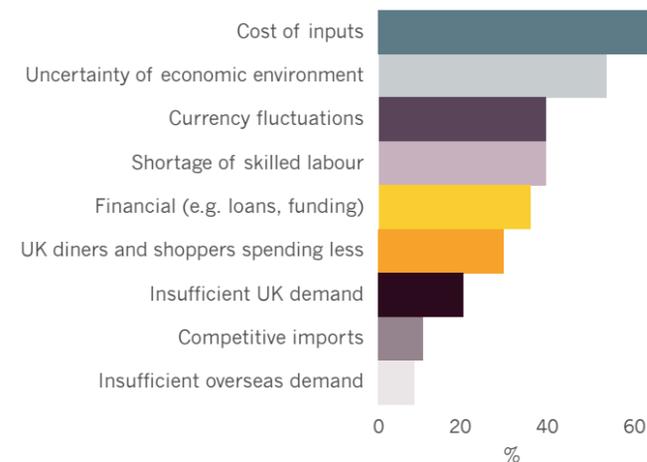
Which areas will be the focus of your innovation investment (including R&D) over the next 12 months?



Excluding seasonal variations what net changes to staff levels do you forecast in the next 12 months?



What factors will limit your ability to increase business activity in the next 12 months?



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