



## Outlook and Opportunities for Growth in the California Food and Beverage Industry

The food and beverage industry is one that can thrive even in the face of a struggling economy. It is, however, important for business owners and executives to know how to navigate financial, market and operational challenges to ensure a strong revenue stream and long-term viability. While some companies are successful operating at the status quo, it is critical for most to look both inward and outward to determine areas for improvement. Looking inward, companies can improve strategic planning, financial analysis, operational systems and product development. Looking outward, companies can partner with industry experts and advisors as well as participating in benchmarking programs to learn best practices from marketplace leaders.

Green Hasson Janks recently conducted a targeted survey of food industry business owners and executives to explore topics such as business growth, pricing issues, new-business strategies and financial management. This year's survey results show that owners are cautiously optimistic about the growth of their businesses in 2012. Companies are enjoying small to moderate revenue growth and are optimistic about additional increases in 2012. While financing and cash flow were the chief concerns in 2011, increased competition is at the forefront of respondents' minds for 2012. Respondents indicated that their primary sources of new business in 2011 came from new product offerings and increased sales from existing customers. Although 80 percent of respondents indicated that they reviewed sales figures monthly, more than half admitted that they do not employ a formal business plan. Furthermore, nearly a third of the respondents indicated that they do not operate using a formal annual budget. Food and beverage executives will need to take strong measures to ensure their growth in a difficult economic climate. Careful financial analysis, strategic planning and a commitment to innovation are keys to ensuring the industry's success. This report presents key factors that affected the industry in 2011 as well as a providing an outlook on the industry for 2012. Combining survey results with industry statistics, the paper provides a summary of industry trends, concerns and also offers real-life solutions that companies can employ to assure their survival.

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## BACKGROUND INFORMATION

The U.S. retail food and beverage industry represents \$1.5 trillion in annual revenue (Plunkett Research Ltd.). Typically divided into segments, the food and beverage industry consists of production and distribution. While most Americans agree that the economy is still in crisis, the food and beverage industry may be one area that continues to maintain or increase market share. In fact, the Dow Jones U.S. Food and Beverage Market Watch reports a revenue increase of seven percent over the last year<sup>1</sup>. However, food-processing companies have been forced to become more innovative in decreasing the cost of products and attracting new customers while still maintaining or increasing profit margins.

## INDUSTRY TRENDS

1. The economy is a driving force in consumer choices. In the face of the struggling economy, consumers continue to look to cut expenses wherever possible. Some of the ways that this has affected the food and beverage industry is through the purchase of generic or off-brand food products, increased cooking at home and decreased dining out. The emphasis on home cooking may be one reason that the industry has enjoyed a slight gain.
2. Rising raw material costs are a major factor to the food and beverage industry. As commodity prices rise, food companies are forced to increase pricing. However, if the market can't bear increased prices, revenue remains level and profits decrease.



3. Increased competition in the food and beverage industry directly impacts sales and profitability. With the competition keeping sales prices in check, companies are forced to innovate which can be expensive and difficult.
4. Emerging markets offer areas for innovation and increased market penetration. For example, the Latino sector is the fastest growing demographic in the country, expected to grow 34 percent between 2010 and 2020<sup>2</sup>. Additionally, the epidemic levels of obesity in America continue to impact the food and beverage industry through an increased demand for healthy foods companies that support healthy lifestyles.

## KEY FINDINGS

The Green Hasson Janks survey is the first of its kind to target California-based food and beverage companies. Half of respondents worked in the areas of beverage (non-dairy) and meat/poultry/seafood and most focus sales in Southern California. With an average annual revenue of \$53.8 million, the majority of companies (67 percent) are family businesses. Respondents have enjoyed an average of more than 25 years in business. With

an average of 102 full-time employees, companies experienced a modest one percent increase in employee numbers between 2010 and 2011.

- Most executives (58 percent) reported that gross annual sales increased less than eight percent from 2010 to 2011.
- 91 percent of executives report modest profit increases from 2010 to 2011 of an average of 9.17 percent while only nine percent of companies indicated a loss of an average of 5.2 percent.
- 91 percent of executives indicated that they had increased prices at least once during 2011 with an average increase of less than six percent.
- One-third of executives anticipate that gross profit margins for 2012 will remain level while 66 percent anticipate an average growth of 12.98 percent.
- 27 percent of executives expect dramatic net profit increases for 2012 while the remainder anticipates more modest increases of 11.33 percent.
- 82 percent of executives do not anticipate making an acquisition in the next five years and 55 percent anticipate a sale or merger by 2017.



## INDUSTRY CHALLENGES

Green Hasson Janks asked executives to rank their top challenges for 2011 and looking forward to 2012. While financing and cost of fuel are key concerns for the industry, increased competition is the chief concern for executives this year.

### Financing and Cash Flow

More than 70 percent of executives cited financing and cash flow as a primary concern for both 2011 and 2012. With banks limiting the amount of financing available to small businesses, companies may find it difficult to obtain the level of financing that they need to succeed. Executives are seeking investor funding and working with vendors to increase lines of credit to compensate for decreased funds available from traditional banking sources.

Internally, companies are faced with rising raw materials prices, increased health and general insurance rates and mounting payroll expenses. When coupled with stalled sales revenue from an inability to increase prices, companies find their bottom line edging downward. Some companies are finding success by executing longer-term contracts or regularly evaluating supply sources. Others focus on bringing in new sales staff with existing sales relationships.

### Cost of Fuel (Utilities/Logistics)

With California gas prices significantly above the national average, California-based companies find fuel costs especially challenging. Executives report that while they have “no control over fuel costs,” they have “consolidated routes to cut mileage.”

Companies are also focusing on “quantity purchasing” and lowering costs through automation. For those companies with national distribution, “placing inventory in strategic locations throughout the United States” is effective in reducing logistical costs.

### Increased Competition

With the food and beverage industry enjoying modest gains in the face of economic crisis, companies will find it both effective and profitable to establish brand recognition amidst growing numbers of competitors. Executives report “updating product and pricing to address the competition,” but only 40 percent plan increase research and development spending. With increased competition comes limitation on companies’ abilities to raise sales prices. Most executives believe that they can’t raise prices above those of the competition. Therefore, innovation and new product development are essential in order to penetrate new sectors and increase revenue.

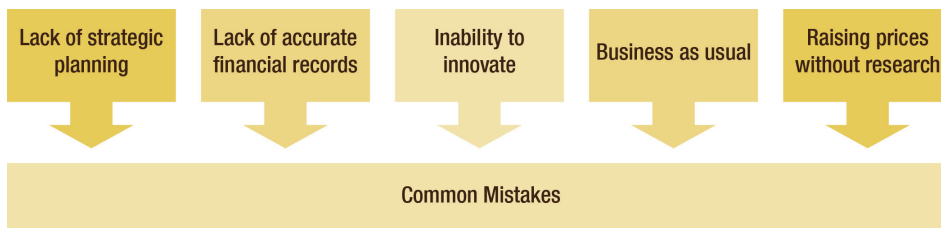
### Government Regulations and Food Safety

While executives consistently ranked government regulations and food safety lower in their 2011 and 2012 concerns, companies should continually address changing federal regulations. Another concern is loss of consumer confidence in the wake of incidences of unsafe food or contamination. Research has shown that consumer trust in their food supply is declining. Therefore, it is important for companies to ensure proper food sourcing while limiting contamination and spoilage as a measure to increase consumer confidence. Furthermore, it is essential for executives to thoroughly prepare their companies for future regulatory changes.



Challenges	2011 Ranking	2012 Ranking
Financing and Cash Flow	1	3
Cost of Fuel (Utilities/Logistics)	2	2
Increased Competition	3	1
Government Regulations/Food Safety	4	4
Cost of Labor (Employee Retention)	5	5

## FIVE COMMON MISTAKES



Frequently, businesses make one or more of these common mistakes:

1. They fail to engage in strategic planning. More than half (55 percent) of executives admitted to operating without a formal business plan. When it comes to business, the lack of a strategic business plan is a recipe for failure.
2. They lack accurate financial records. Without detailed financial records by product and division, companies cannot determine accurate profit centers or loss leaders.
3. They do not have the ability to innovate. Successful companies invest in change. Innovation comes in the form of developing new products, penetrating new markets or targeting new consumers. Companies that don't move into emerging markets such as the Hispanic or health food markets are destined to fail.
4. They operate with a business-as-usual mentality. Companies with a long history of operational success may fall into the common trap of producing the same products with the same approach simply because it is what is familiar and comfortable.
5. They raise prices without research. Companies that raise prices without fully researching the ramifications may be faced with decreased sales revenue. Although it's been several years since prices have been raised or because the competition has increased its selling prices, the market may not bear the increased cost. Furthermore, if products have been consistently underpriced, consumers may not tolerate a sudden price increase.



## GREEN HASSON JANKS STRATEGIES FOR SUCCESS

Companies that want to thrive in a struggling economy and beyond need to commit to four key strategies. While these strategies may require additional resources in terms of time and finances, companies can expect success when they: 1) commit to planning for the future; 2) carefully evaluate their finances; 3) obtain outside help when it is appropriate; 4) look to others within their industry to benchmark performance.

**1. Strategic planning.** It is essential to create short-term (six months) and long-term (five to ten years) plans. In addition to defining a company's purpose and vision, a strategic plan includes specific goals and financial targets as well as the steps necessary to achieve those goals. A key tool in strategic planning is a SWOT analysis (strengths, weaknesses, opportunities and threats) that can help a company determine areas for focus and improvement. While the specifics of a strategic plan may be dynamic, adjusted as situations change, the plan should address high-level initiatives that drive every division of the company. Plans should be reviewed regularly to ensure compliance and allow adjustments as needed.

**2. Accurate financial records.** The majority (73 percent) of executives report that their companies prepare annual budgets or forecasts and nearly 90 percent say that they review these statements on a monthly basis. However, incomplete or inaccurate financial statements can lead to decisions that may detrimentally affect the



bottom line. Statements should include profit and loss analysis by product as well as reports by division. While it is essential to review complete reports monthly and quarterly, more frequent review of key indicators will keep decision makers aware of any sales or expense trends immediately. These daily “dashboard” reports should include four or five key indicators and may include daily sales, labor per day, labor per hour, daily cash sales, daily gross profit or other key figures specific to the company.

- 3. Use consultants where appropriate.** While we don't recommend frivolously committing resources to outside consultants, the use of experts where appropriate can benefit the bottom line. Marketing consultants can help develop strategies for branding and advertising. Logistical experts provide advice on operational issues including supply chain, distribution and warehousing. Financial consultants can assist with strategic planning, budgeting, risk management, financial reporting and taxes. Since 90 percent of companies surveyed use outside consultants, it is essential to make sure the consultants in place are the most effective, efficient and appropriate based on the company's goals.
- 4. Benchmark against others.** Companies should continually look to competitors and industry leaders to compare business processes and performance. Additionally, companies may learn best practices from success stories or failures. Benchmarking may take place during a seminar, conference or smaller peer-group gatherings. Information may also be garnered by reading trade periodicals. An open dialogue with competitors can help expose emerging trends, underserved markets. Areas benchmarked may include processes, finances, performance, products, strategy and operations.

## SUMMARY AND CONCLUSION

In the extremely competitive food and beverage industry, companies are cautious in the wake of a slowly improving market. While sales appear promising, the industry is faced with rising commodity costs, increased fuel prices and fluctuating raw-material expenses. Other trends include increased competition, increased regulation and growing markets such as Hispanic and natural products. Survey results indicate that revenues were up in 2011 and respondents are optimistic that sales will continue to rise in the next year. However, to remain afloat, it is important for companies to look for new and innovative ways to retain or increase market share in an era of weakened consumer demand. Food and beverage business owners are faced with a Catch 22: They need to spend money to develop new products and remain relevant, yet financial institutions are reluctant to extend financing. Through careful financial analysis, companies can determine which products are profitable, where costs can be cut and where money should be spent to ensure growth in the future.

This publication provides information and comments on current accounting issues and developments. However it is not a comprehensive analysis of the subject matter covered and is not intended to provide accounting or guidance with respect to matters addressed above. All relevant facts and circumstances, including the associated authoritative accounting guidance and literature should be reviewed to arrive at conclusions that comply with matters addressed above. This material was not intended or written to be used, and a taxpayer cannot use it, for the purpose of avoiding United States federal or other penalties or of promoting, marketing or recommending to another party any tax-related matters.

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<sup>1</sup> ([http://www.marketwatch.com/tools/industry/focus.asp?bcind\\_ind=3500&bcind\\_sid=215763](http://www.marketwatch.com/tools/industry/focus.asp?bcind_ind=3500&bcind_sid=215763))

<sup>2</sup> United States Census Bureau

### About the Author

Donald J. Snyder is a partner at Green Hasson Janks and heads the firm's food and beverage division. Donald has more than 25 years experience in public accounting and chairs the firm's Accounting and Auditing Department, as well as the Quality Control Department. He provides audit, accounting and consulting service to clients in numerous industries, including manufacturing, wholesale/distribution, restaurant, food and beverage, nonprofit and technology. He is a well-known business consultant in the food distribution, food processing and manufacturing industries. A popular industry speaker, Donald also writes for the firm's quarterly Food Digest newsletter and hosts a number of food and beverage networking groups.

Donald is involved in assisting clients with designing and assessing their internal accounting controls and has been a frequent lecturer in this area. He has also written several articles on the subject of fraud prevention and detection in the work place. In September 2011, Donald was nominated for a San Fernando Valley Business Journal award as one of the “Valley's Most Trusted Advisors.”

Donald holds a Bachelor of Science degree in Administration with emphasis in Accounting from the University of Colorado. He is a member of the California Society of Certified Public Accountants and the American Institute of CPAs.

### About Green Hasson Janks

Founded in 1953, Green Hasson Janks is one of the oldest independent accounting firms on the west side of Los Angeles. Ranked as a top-20 largest accounting firm on the Los Angeles Business Journal's Book of Lists, the firm has 13 partners and approximately 100 staff members that serve over 3,000 clients.

The firm is a member of the American Institute of Certified Public Accountants (AICPA), the AICPA Governmental Audit Quality Center (GAQC), the California Society of CPAs and the California Association of Nonprofits (CAN) and the Public Company Accounting Oversight Board (PCAOB).

Green Hasson Janks is also an independent member of HLB International, a worldwide organization of professional accounting firms and business advisors represented in over 100 countries. This affiliation provides access to the subject-matter experts of other member firms in most major cities around the world. Green Hasson Janks is the exclusive member firm of HLB in Los Angeles County.

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