Green
Hasson
Janks
&
Food
Digest

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Outlook and Opportunity for Growth in the California Food & Beverage Industry

2012 Green Hasson Janks Food & Beverage Survey Results

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 and through 2013. We presented the results of this survey at a food conference recently held in October 2012 that was attended by over 150 people. In this food digest issue, we will summarize the results of the survey broken out in the following areas: general, financial, challenges facing the industry, and M&A activity.

General Company Information

The Green Hasson Janks survey is the first of its kind to target California-based food and beverage companies. While the survey results indicated that several companies generated revenues internationally, the great majority of the companies generated their revenue from sales both in Southern California and nationally. Approximately 67% of the respondents are family owned, privately held businesses. The average size of these businesses was approximately $53 million in revenue and had over 100 employees. In addition, the companies that participated in our survey had food specialties which included, but were not limited to meat, seafood, beverage, produce, baked goods and snack food.

Financial Statistics

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 last year and the organic and natural line are up over 9% in 2012. 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. The results of our survey indicated that most executives (58 percent) reported that gross annual sales increased less than eight percent from 2010 to 2011. 91 percent of executives reported modest profit increases from 2010 to 2011 of an average of 9.1 percent while only nine percent of companies indicated a loss of an average of 5 percent. In addition, 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 12.9 percent. Lastly, 27 percent of executives expect dramatic net profit increases for 2012 while the remainder anticipates more modest increases of 11.3 percent.

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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. 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. 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.

M&A Activity

On the M&A front, although acquisition activity in this sector has had a modest decrease from the prior year, continued improvement in economic fundamentals and anticipated growth in on-trend niches and private label is expected to serve as a strong foundation to drive growth and M&A activity in the food and beverage industry into 2013. Our survey results indicated that 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.

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 several years. 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.

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The American Taxpayer Relief Act of 2012 and the Food & Beverage Industry

The new year brought yet another major piece of tax legislation. The American Taxpayer Relief Act of 2012 (ATRA) which was actually passed on January 2, 2013, includes a number of provisions important to the food and beverage industry. For the most part, the provisions affecting food and beverage industry included in the ATRA was renewing or extending existing provisions. In this issue of Food Digest, we wanted to highlight certain aspects of these provisions affecting the industry.

Depreciation

The 50% bonus depreciation has been extended through 2013 (2014 for long production property). Of importance to the restaurant industry, the 15-year straight-line cost recovery for qualified leasehold improvements, restaurant buildings and improvements, and retail improvements has been retroactively extended through 2013. Finally, section 179 expensing amount of $500,000 has been extended through 2013.

Research and development (R&D) tax credit

Many companies in the food and beverage industry have activities that qualify for the R&D tax credit. The credit, which had expired at the end of 2011, was retroactively reinstated for 2012 and extended through Dec. 31, 2013.

The R&D tax credit provides taxpayers with a dollar for dollar reduction in tax and is determined based on a company's investment in technology and employment within the United States

Food Inventory Contributions.

ATRA retroactively extends the enhanced deduction for donation of "apparently wholesome food" (intended for human consumption) for the period starting January 1, 2012 through December 31, 2013. The provision allows a C corporation to claim a charitable deduction equal to the lesser of (1) 150% of the cost of the inventory donated, or (2) twice the cost basis of the inventory.

Work Opportunity Tax Credit

ATRA extends the Work Opportunity Tax Credit (WOTC) expiration date from December 31, 2011 to December 31, 2013. The WOTC is a federal income tax credit of up to $2,400 for each qualified newly hired employee that falls into one of eight targeted groups. These groups include members of families receiving benefits under the Temporary Assistance to Needy Families program, designated community residents, vocational rehabilitation referrals, qualified ex-felons, qualified summer youth employees, qualified food and nutrition recipients, qualified Supplemental Security Income recipients, and long-term family assistance recipients.

ATRA also extends through December 31, 2013 the WOTC available to businesses that hire qualified veterans. The maximum federal income tax credit amount for employers that hire qualified veterans ranges from $2,400 - $9,600 per qualified veteran hired.

To submit future topics or provide feedback, please contact Kari Schott at kschott@greenhassonjanks.com

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