



BAKERY INDUSTRY: A PARADOX

Farrelly & Mitchell Executive Report

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Food & Agri-Business Specialists

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REAL INDUSTRY EXPERTISE

FROM STRATEGY TO IMPLEMENTATION



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Farrelly & Mitchell

Farrelly & Mitchell is pleased to present **Bakery Industry: A Paradox**. In this report we offer insights into how bakery companies can grow and capture market share within a highly competitive and paradoxical market.

Our extensive advisory experience supporting companies in bakery markets around the world gives us a clear insight into the many challenges facing businesses in this industry. As well as drawing from our own hands-on experience working with a range of businesses from large multinationals to SMEs, we have pulled together information from various published sources to generate our unique perspective on the future of bakery products.

The industry remains highly competitive with health trends dominating the global food market, and the bakery industry.

While consumers want healthy bakery products, they also want to indulge and do not want to compromise on taste. For many consumers, variety is the spice of life and demand is growing for innovative new recipes and variations of old ones.

In our experience as international food and agribusiness specialists, we know that understanding the consumer is not enough by itself. In order to remain competitive, commercial operations need be driven by both market and industry practicalities. In the highly competitive baked goods sector, employing innovations that improve processes and help reduce costs are just as important as product innovations.

I would like to thank our research team based in Europe and MEA. As always we welcome your feedback.

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If you would like to discuss any aspect of this report, please contact us.





Going forward, the companies that can balance the health concerns of their customers with expectations around indulgence are the ones most likely to successfully capture growth in the market.

The growth outlook for the bakery industry is positive, however, market growth is driven by rapidly evolving consumer preferences. These preferences are, in turn, driven by market trends that are somewhat paradoxical in their nature e.g. increasing health consciousness among consumers and greater demand for indulgence foods.

The most successful companies are those that are responsive to changing market demands. Bakery companies need to listen to their customers, and adjust their product mix accordingly.

Going forward, the companies that can balance the health concerns of their customers with expectations around indulgence are the ones most likely to successfully capture growth in the market. However, that alone is not enough to ensure success.

Variety in a company's product mix in order to satisfy changes in consumers' day to day needs and desires is also essential. In addition, it is important that company's effectively communicate their products' features to their customers to drive sales. This is especially true as regards consumer health, as a lot of consumers wrongly believe that certain bakery products are unhealthy.

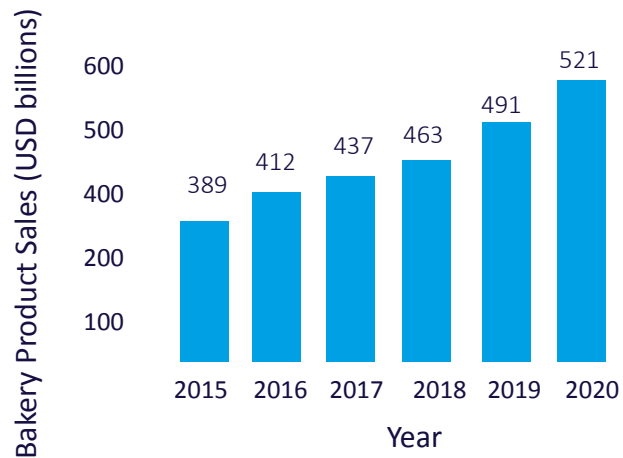
While having a market orientation can position the company for success, the foundations must also be solid. The industry is highly competitive and efficient production is essential.

Technological innovations in hardware and software for the industry continue to push boundaries. The adoption of these innovations, were practical, can help companies reduce costs and remain competitive.

Companies must explore all bases from product to process innovations to ensure growth in sales and profits. In this report, we look at the bakery industry, examining the main factors driving growth in the market and providing our expert perspective on how companies can stay on top the competition.

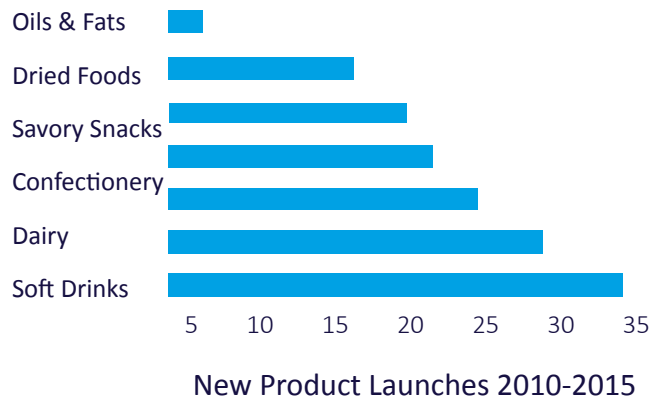


Fig 1: Global Bakery Product Sales 2015 - 2020



Source: Euromonitor International 2016, Farrelly & Mitchell Research

Fig 2: Global Grocery Retail - New Product Launches in Select Food Categories



Source: Datamonitor

The outlook for the bakery industry is generally positive, with the value of global sales expected to grow at a CAGR of 6% to reach \$521 billion in 2020.

Bread and biscuits remain the dominant categories, with cakes and pastries the fastest growing. Geographically, growth in the industry is driven by increased consumption in emerging and developing countries. In mature markets, demand for traditional bakery products or the staples, is declining, while sales of “healthy” baked goods with natural and organic ingredients are growing.

One of the key features of the market for bakery products is the rapidly evolving nature of consumer preferences. Evolving consumer preferences contribute to the sector having one of the highest levels of product innovation in the food industry - please see Figure 2.

In mature markets, growth is typically driven by evolving lifestyles and increasing demand for comfort food. Among the key trends impacting the industry in recent times have been increased health consciousness among consumers and growth in consumption of indulgence food. In the mind’s eye of many consumers, bakery products are viewed as unhealthy.

At the same time, paradoxically, consumers have a strong desire for indulgence foods. This is particularly important in the bakery industry where indulgence foods represent a significant proportion of production. Resolving the health vs. indulgence paradox represents a significant opportunity for manufacturers. Doing so requires marrying health and indulgence through product and technical innovations.



What is Driving Consumer Preference?



Fig 3: Driving Forces of Consumer Preference for Baked Goods



While consumer preferences vary by geographic location, globally, the four factors outlined in Figure 3 are the main criteria consumers consider when purchasing bakery products.

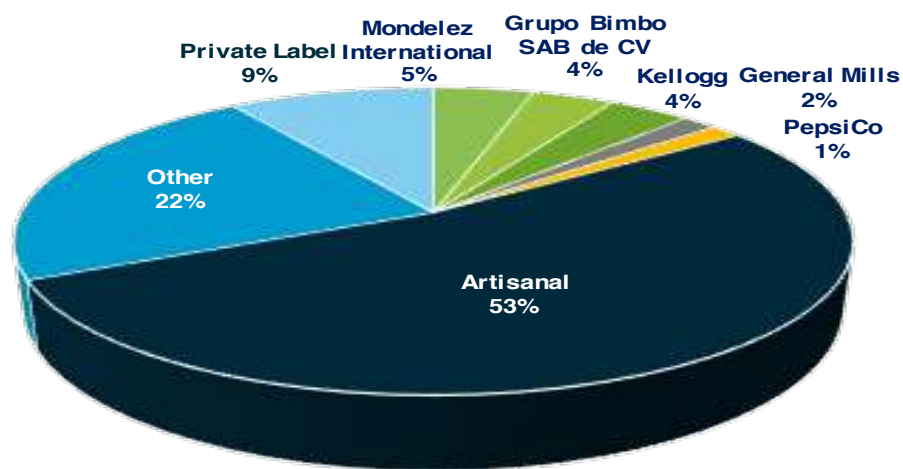
Consumers prefer freshness, taste/flavour and price over health benefits. This indicates that despite the ever increasing importance of health benefits, bakery products are at the pleasure end of the pleasure-sustenance spectrum in the minds of consumers.

Flavours and freshness are the key considerations in the consumers' perspective. This makes the bakery industry somewhat paradoxical.

Companies need to ensure that their products provide both indulgence and adequate sustenance. It also contributes to the continued fragmentation in the global bakery market where artisanal bakeries dominate and the top five companies in the industry only hold just over 15% of sales - please see Figure 4.

This, of course, does not mean that health concerns do not drive growth in the industry. In fact, with regards to consumer preferences; health factors are almost always ranked above other factors such as product origin, brand, package size, tradition, production method employed (i.e. artisan or mass production) and presence or lack thereof of specific ingredients.

Fig 4: Global Market Share – Top 5 Bakery Companies



Source: Euromonitor International 2016



While consumers want healthier products in greater varieties, they are not sure what exactly they want beyond ‘healthy’, or even what exactly ‘healthy’ means.

Health consciousness is a rising trend globally and is impacting all food and drink product categories. It has resulted in consumers feeling guilty and being overly cautious when it comes to consumption of bakery products.

For example, a survey carried out by Brennan’s Bread on the consumption of white bread in Ireland found that consumers were largely misinformed with widespread negative perceptions around white bread. Despite over 80% of respondents enjoying the taste of white bread, the survey found that:

- Over a third of those surveyed said they don’t eat it because they think it is bad for them;
- A quarter of people revealed that they don’t eat it because they think white bread is ‘too fattening’; and
- A further 21% stated that it makes them feel bloated.

This is a common theme in many western countries, where studies consistently find large portions of the population report feelings of guilt about consuming white bread.

Bakery products are increasingly treated less as a regular part of diet or daily routine, and

more as an occasional treat, such as weekend brunches.

Influenced by rising health consciousness, demand for healthier and nutritional fortified bread has increased and the fastest growing brands are those that specialise in innovative “healthy” bakery products, made from high quality ingredients and that target demand for “free-from” and convenience food.

However, manufacturers need to ensure that they effectively communicate their product messages to consumers. While consumers want healthier products in greater varieties, they are not sure what exactly they want beyond ‘healthy’, or even what exactly ‘healthy’ means. Effective marketing can help consumers discover new products and features, but also, and perhaps more importantly, communicate the health benefits of their products.

This requires an in-depth understanding of how consumers think when making purchasing decisions as well as knowledge of the best communications channels to use to reach consumers. In addition, there is significant potential for manufacturers to grow sales of these traditional bakery products that have been in decline in recent years. This can be done by educating misinformed consumers and using simple flavours and clean ingredients.

Variety is Key



Bakery manufacturers need to be aware that consumption patterns are changing. In particular, consumers are eating a greater variety of food products.

In the baked good market, particularly when treating themselves, consumers want to experiment through the consumption of small servings of different baked products. They also want to indulge without negatively impacting their health.

Most bakery products purchases are planned and relatively routine. However, baked goods are closely related to snacking and treating behaviours, and are more likely to be purchased on impulse than breads - please see Figure 5.

In addition, consumption patterns also differ over relatively short time frames. This is evident in the desire for weekday convenience and weekend experience.

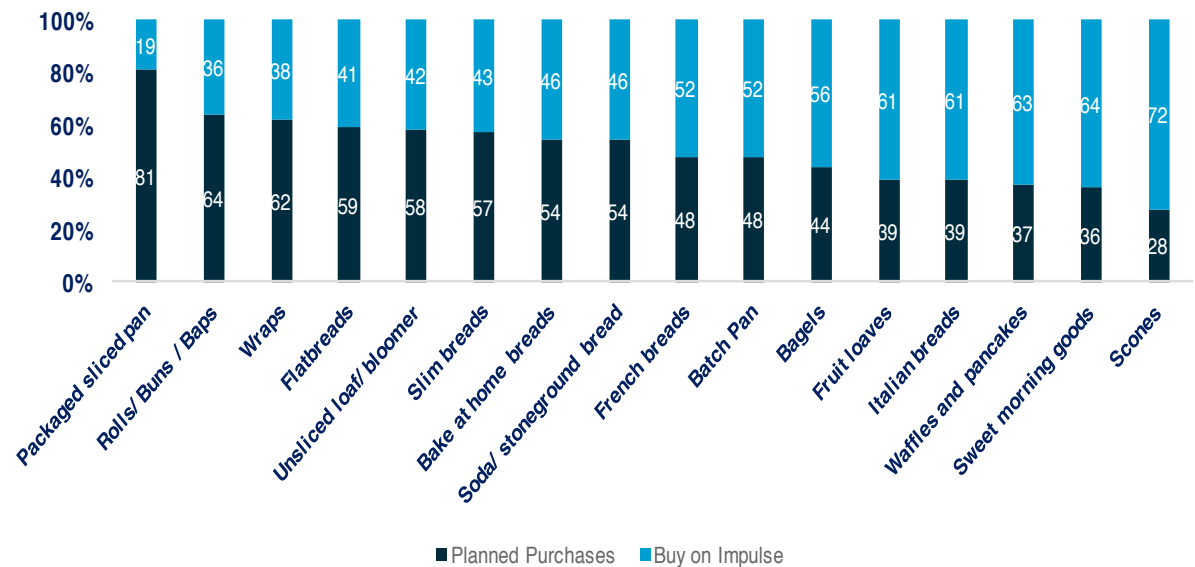
Consumers increasingly lead busy lifestyles with limited time to shop for food during the week. This has led to the increased demand for convenient solutions to consumers' food

consumption needs. Portable and snackable options continue to be on the rise, while the global grab-and-go breakfast market is set to expand by 46% by 2026.

Bakery consumption has traditionally been more of a functional task to get sustenance, rather than for indulgence purposes. It remains so during the week, when consumers want quick and practical solutions that are also familiar, convenient and good value.

Additional product benefits or attributes that add a little excitement to their routine can sway the consumer away from their usual product purchases. With more time on their hands during the weekend, consumers are able to look for indulgence and reward for their week's hard work. Therefore, weekend baked good purchases are more exploratory and sophisticated. Value is still somewhat important but consumers are willing to pay more for the experience and variety.

Fig 5: Impulse or Planned Purchases by Consumers in England – Bread and Baked Goods



Source: Bord Bia (Irish Food Board)



The desire for variety in the bakery market is substantial and likely to continue to grow into the future.

Companies who want to capture a bigger slice of the market need to understand this so that they can appropriately tailor their product offering and marketing communication efforts. To date, bakery companies have failed to influence the consumers' decision-making process to the fullest extent. This is mainly due to lack of investment in consumer research and product innovation.

The desire for variety in the bakery market is substantial and likely to continue to grow into the future. Companies must have the flexibility to continuously wow consumers through tailored new product innovations, while maintaining a core product range that meets weekday needs. Without this variety in a company's product mix, the core range suffers and become easily substitutable.





Employing technical innovations that improve processes and help reduce costs can be just as important as tailored product innovations in the bakery industry.

A major challenge for the bakery industry has always been the clash of the need for control systems and the artistry of baking. Nonetheless, a competitive market encourages bakery companies to reduce costs and increase margins through automation.

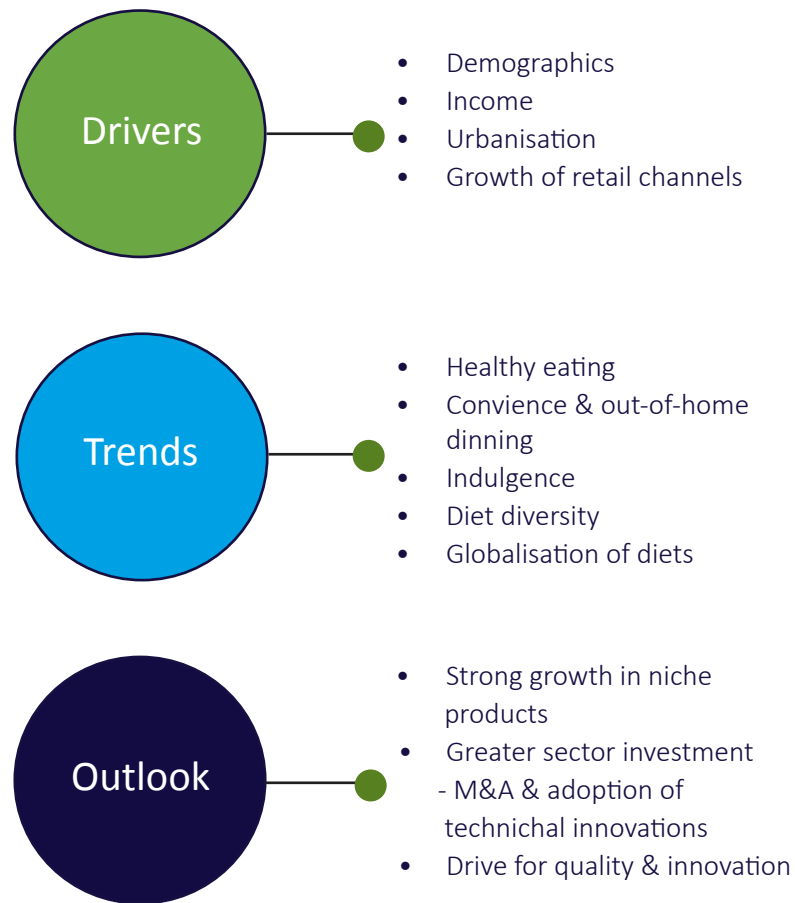
Employing technical innovations that improve processes and help reduce costs can be just as important as tailored product innovations in the bakery industry. Progress in machine intelligence is becoming more central to staying technically innovative for many food companies, including industrial bakeries.

Recent years have seen some major technical innovations for the bakery industry. One disruptively innovative example comes from PreciBake GmbH, a German software developer. Their technology, also in use in the automotive sector, helps regulate and refine the production process through sensors and software for bakery equipment. As the software collects data, the more informed the program's decisions become almost allowing "the machinery to program itself".

Another example is a suite of sensor-driven software and hardware packages from Mecatherm SAS, a Paris-based fabricator of integrated baking lines. The suite includes:

- A vertical proofer and a hybrid oven that combines cyclothermic and impingement heating;
- A maintenance pack that provides condition-monitoring data that enable a predictive approach to machine maintenance;
- A traceability pack which captures electronic signatures for every human input; and
- An energy and exhaust monitoring system to benchmark consumption of gas, electricity, compressed air and steam.

The adoption of these types of innovations can significantly reduce costs and increase plant efficiency.



The key conclusions from our research are the following:

- It has never been more important for bakery manufacturers to listen to their customers and adapt their product mix accordingly;
- Resolving the health vs. indulgence paradox represents a significant opportunity for manufacturers to grow sales and achieve success;
- Offering a variety of products is very important to cater to the ever-busy consumers, it is not by itself enough. Companies must also be able to communicate the features of their products to their customers;
- An industry this competitive requires pulling all means for success: Offering a variety of innovative products is not enough. To be profitable, companies must be technically innovative as well.





About us

Farrelly & Mitchell empower some of the world's most ambitious companies and agencies to make the right decisions. With expert insight, local market intelligence and airtight recommendations, we build and implement sustainable strategies that allow our clients to restructure, transform and grow.

We have the hands-on industry experience and expertise, which we combine with local market insight and contacts to help our agribusiness, food and beverage clients to increase profits and improve efficiencies.

What makes us different?

We go above and beyond traditional consultants. As an international management consultancy, we specialise in the global food and agribusiness industry, with a particular focus on the implementation or execution of our recommendations. So we are committed to working with our clients, not just in the development or planning phase of a project, but importantly in its full implementation.

Food an agribusiness specialists

We understand food and agribusiness; we built our experience in this sector, and we employ the best global talent to provide in-depth solutions by addressing real problems sustainably and creating new opportunities for clients.

For the past decade, we have worked with clients across the globe and generated measurable results. We have worked on mandates across every link of the food and agribusiness value chain from large-scale farming operations to food or beverage manufacturing, distribution, retail and hospitality.

Each member of our team of over 200 experienced consultants has worked in industry at an operational and executive level.

We work globally with significant experience in Europe, Middle East and African markets.

Why partner with Farrelly & Mitchell?

Our team has worked at operational and strategic levels all over the European, Middle Eastern, and broader international food, beverage and agribusiness sectors. We have seen projects through from paddock to plate.

We understand the opportunities presented by the growth of the food, beverage and agribusiness sectors, in the Gulf region and across the globe. We work with primary producers, manufacturers, distributors and retailers.

If you are you looking to grow or expand your business, improve efficiency or quality control, or are buying or selling a business, get in touch, and let Farrelly & Mitchell become your project partners.

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