# Why capital investment should be a top priority for management teams in the Agrifoods sector

In this article we consider why senior business leaders in the Agrifoods sector should be turning their attention to capital investment to drive operational efficiencies, expand capacity and improve their sustainability.

It is clear from our recent interactions with businesses in the sector that the management of cash has been a key priority over the last few years given the confluence of external events which have impacted the sector. The supply chain disturbances and inflationary pressures which have sprung from these events (e.g the war in Ukraine) continue to have wide-ranging impacts.

We have seen many instances where capital projects were delayed, reshaped, or even cancelled entirely as cash flows were preserved to provide a buffer against future uncertainty. In other instances, this cash was diverted to support increased working capital demands as a function of higher commodity/raw material prices.

With food inflation (and headline CPI) appearing to be on a downward trajectory and interest rates beginning to stabilise in response, we are starting to see management attention moving away from an inward facing, day to day trading focus, to strategic growth opportunities which requires fixed-asset investment.

However, many capital projects which made sense two to three years ago are now no longer relevant given current consumer/ economic trends. Furthermore, the return-on-investment arithmetic may no longer work, as a function of the increased cost of debt and higher project/development costs.

Against this backdrop, we are seeing some hesitation from management teams to make new investment decisions. Whilst clearly any new capex activity needs to be carefully considered, other leadership teams are moving forward with plans at pace. For those doing this, they have accepted the fact there is going to be a higher baseline level of uncertainty going forward, many of the trading headwinds are outside their control and, in some cases, urgent change is required to compete.

Increasing automation by replacing/renewing old equipment to reduce costs and improve productivity is dominating discussions, with labour availability and cost being the key drivers. A survey by BDO in late 2023 further evidences this observation.

This survey revealed that 39% of food and drink businesses which responded are expecting to increase capex in the next 12 months, with a quarter of those surveyed expecting to make investments in automation (and digitisation) to support profit growth.

The new National Living Wage ('NLW') which takes effect in April 2024, increasing from £10.42 per hour to £11.44, represents a substantial increase to a sector which is labour-intensive – in April 2021 this figure was £8.91. Labour availability also remains a persistent issue which, in the case of food manufacturing, is laid bare by a recent FDF report which shows that vacancies per 100 employees was 6.5% in 3Q23. This was more than double the UK average (2.9%) and the wider manufacturing sector (3.1%).

Whilst automation is a key theme, we are also seeing an increasing number of businesses investing in sustainability projects, such as carbon mitigation activities (e.g. installation of solar panels, fleet electrification etc). These businesses understand that sustainability is becoming a key driver in winning new business and enhancing market reputation.

**Closing thoughts:**
In summary, we would encourage management teams to take a long-term view when considering new capital investments. Whilst it is not clear on how NLW and labour availability will evolve, the direction of travel appears clear. This, coupled with an environment where higher operating costs are likely to be the norm e.g. energy (a recent PwC survey saw 81% of respondents from across UK industry expecting energy prices to increase in the next 2 years) should make capital projects easier to justify financially. In planning for the future, sustainability should also not be overlooked. Capital investment to support this change will undoubtedly improve long-term competitiveness, bottom-line potential, and operational resilience to those most committed to this activity.

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