Daymon

PRIVATE BRAND MANUFACTURER OUTLOOK SURVEY

2023

EDITORIAL

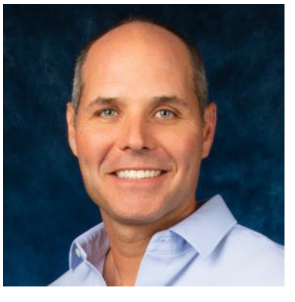
The manufacturing sector has been witnessing a challenging business environment in recent years. Fluctuations in raw material costs, changing trade policies, and geopolitical tensions have disrupted supply chains and resulted in high inflation levels, creating volatility and uncertainty.

Our Daymon Private Brand Manufacturer Outlook Survey, focused on the industry dynamics for, and by, manufacturers that support the Private Brand business - has enabled us to monitor this challenging context since 2022. In this year's edition, we go a little further, trying to understand and anticipate the strategies that manufacturers are seeking globally to sustain growth and profitability.

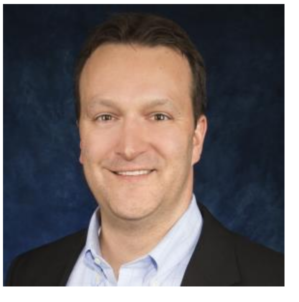
In the midst of a gloomy and uncertain economic context, our Survey suggests that Private Brand has strengthened its role as a solution that supports manufacturers in their quest for success. Investing in Private Brand encourages greater production flexibility, which in turn brings economies of scale and efficiencies and helps expand the market footprint. With retailers prioritizing Private Brands and consumers increasingly looking for Private Brands and more affordable options, manufacturers can leverage these advantages to drive growth and enhance market competitiveness.

The future holds immense potential for private brands to flourish as a key element of the manufacturing landscape.

Daymon, with over 50 years of experience building successful Private Brand programs around the world, has the expertise and capabilities to help manufacturers navigate this challenging context and capitalize on the growth of Private Brands. By leveraging Daymon's solutions, manufacturers can enhance their market position and drive sustainable growth.



Aaron J. Gottlieb, President - Daymon International



Jim Griffin, Executive Vice President - Daymon

EXECUTIVE SUMMARY

The manufacturing sector has been facing significant challenges since 2020, such as the COVID-19 pandemic, supply chain disruptions, labor shortages, shifting consumption patterns, and high levels of inflation (as a consequence of the ongoing conflict in Ukraine, high energy costs and lack of raw materials).

According to our Daymon Private Brand Manufacturer Outlook Survey 2023, ingredient/commodity is the number one cost driver for the industry globally, as pointed out by most manufacturers. Although costs are expected to soften in the next 12 months, energy costs and labor conditions are expected to remain challenges in the long term.

Manufacturers have been showing resilience and adaptability in this challenging business environment, with many diversifying supply chains and negotiating price increases. Manufacturers are also increasingly optimistic about the growth of Private Brands, suggesting that they are particularly appealing during periods of high inflation.

Recognizing the importance of investing to succeed, increasing capacity, as well as investing in product innovation, new product development efficiencies, new technologies (e.g., automation) and sustainability, are key factors that manufacturers are seeking.

Throughout this paper, these and other findings will be explored at a global and regional level.

CONTENTS

METHODOLOGY

An international study was undertaken by Daymon to understand the industry dynamics impacting global manufacturers that support Private Brands. The survey targeted manufacturers across Africa, Europe, Asia, Latin America and the US.

Daymon surveyed 269 manufacturers globally, between April 12 and May 9 of 2023.

KEY TAKEAWAYS

IT HAS BEEN CHALLENGING, AND IT WILL CONTINUE TO BE CHALLENGING

Costs have been high and some challenges are likely to be long-term. Ingredients or commodities stand out as the top cost drivers globally, while long-term concerns will persist regarding energy costs and labor conditions. The geopolitical environment, as well as supply and demand dynamics, collectively contribute to the manufacturing industry's cost fluctuations. These factors directly impact the profitability of manufacturers, who must navigate these challenges by implementing effective risk management strategies, diversifying their supply options, and fostering stronger relationships across the value chain.

THE FUTURE LOOKS BRIGHT FOR PRIVATE BRANDS

Inflationary periods have provided an ideal environment to demonstrate the value and benefits of Private Brands. As manufacturers witness the positive response to Private Brands, both on the consumer and on the retailer side, they are increasingly optimistic about their growth potential and are likely to continue investing in product development and collaborating with retailers to further expand Private Brand in the market. The commitment to continuous improvement and differentiation ensures that Private Brands remain attractive and competitive, paving the way for a bright future.

THE TOP 2 AREAS OF FOCUS GOING FORWARD

In an increasingly competitive and challenging business environment, manufacturers are highly aware of the need to invest in order to remain relevant and bring differentiation to the market. To address these imperatives, manufacturers globally are actively planning strategic investments in the next 12 months. The top two priorities for these investments are product innovation and increasing capacity.

Manufacturers understand that innovation is vital for sustaining growth and meeting evolving consumer demands. They also recognize the importance of optimizing their production capacity, to handle larger order volumes, fulfil customer requirements in a timely manner, achieve economies of scale, and support business expansion strategies, both domestically and internationally.

SUSTAINABILITY IS ON THE AGENDA

Manufacturers globally are increasingly prioritizing sustainability as one of the key focus areas for their investments in the next 12 months. Sustainability has become a business imperative driven by various factors, including environmental concerns, regulatory requirements, changing consumer preferences, and the need to build resilient and responsible supply chains.

Manufacturers are taking the lead in addressing Scope 3 emissions, recognizing that sustainability efforts should extend beyond their own operations. Embracing Scope 3 carbon reduction targets voluntarily demonstrates manufacturers' commitment to sustainability, but it also brings challenges and opportunities. Manufacturers may face complexities in gathering data, collaborating with suppliers, and implementing changes across the value chain. However, these challenges provide opportunities for innovation, efficiency gains, and the development of sustainable and resilient supply chains.

Daymon is well-positioned to help businesses navigate the current challenging environment and leverage future strategies. Based on its in-depth market knowledge and experience in developing Private Brands in all areas of retail, Daymon can assist businesses as they adapt their strategies to the changing industry dynamics.

CHAPTER 1

Challenging business environment

The manufacturing sector is facing unprecedented challenges, driven by a complex mix of economic, social, and technological factors. The BANI framework provides useful context to help us describe the environment we live in - an environment of chaos and unpredictability, where events are extremely difficult to understand and explain.

In 2020, the COVID-19 pandemic disrupted supply chains, caused labor shortages and led to reduced demand for certain products. With factories shutting down in many countries, the flow of goods and materials has been disrupted, leading to shortages and delays. Manufacturers have had to find new sources of raw materials and finished goods, often at a higher cost, to keep their businesses running.

The more troublesome geopolitical environment has added an extra layer of complexity to the manufacturing sector. The ongoing trade tensions between the US and China about unfair trade practices have led to imposed tariffs on many goods, making it more expensive for manufacturers to import and export products.

Furthermore, the ongoing conflict in Ukraine has highlighted not only geopolitical but also economic risks. As tensions between Russia and Western countries increase, there is a growing risk of further disruptions to supply chains, higher prices of key materials, and broader inflationary pressures impacting the manufacturing sector. The conflict impacted the supply of commodities and transportation costs, and disrupted trading routes.

In this chapter, we will explore some of the key market challenges that the manufacturing sector is facing globally.

Main costs drivers

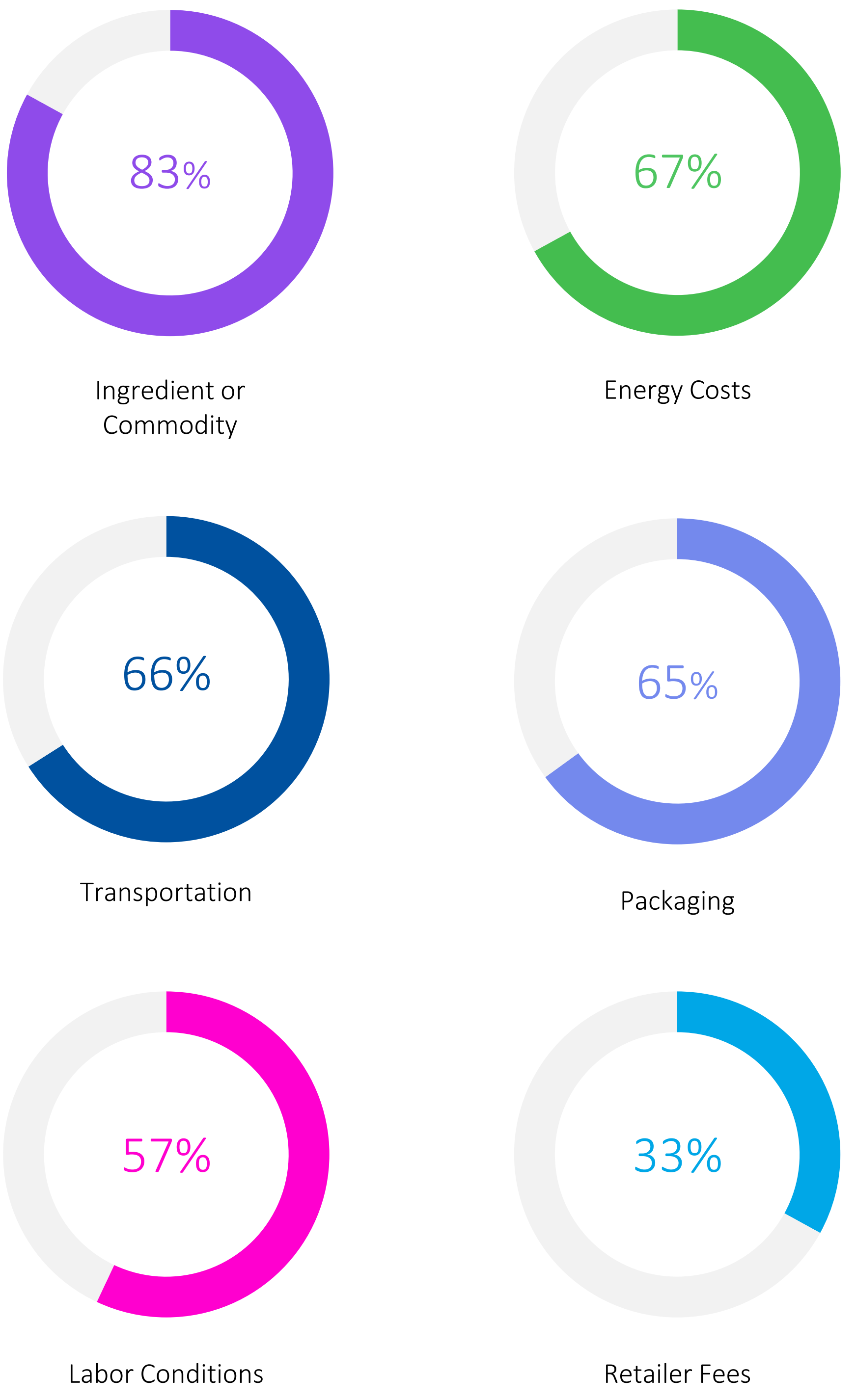
“Increased costs at any stage of the supply chain have a ripple effect on manufacturing operations globally, as the manufacturing sector heavily depends on global supply chains, where resources are sourced from various countries.”

Pedro Carmo, Global Sourcing & Procurement Director (Daymon International), Global

It's not uncommon for costs and prices to increase over time. However, it is clear that an escalation has been observed since 2021 and then again after the onset of the conflict in Ukraine last year.

Most respondents globally say that the costs that increased the most (by more than 11%) in the last 12 months were the costs related to ingredient/ commodities, energy and transport.

Global proportion indicating cost increases in the last 12 months

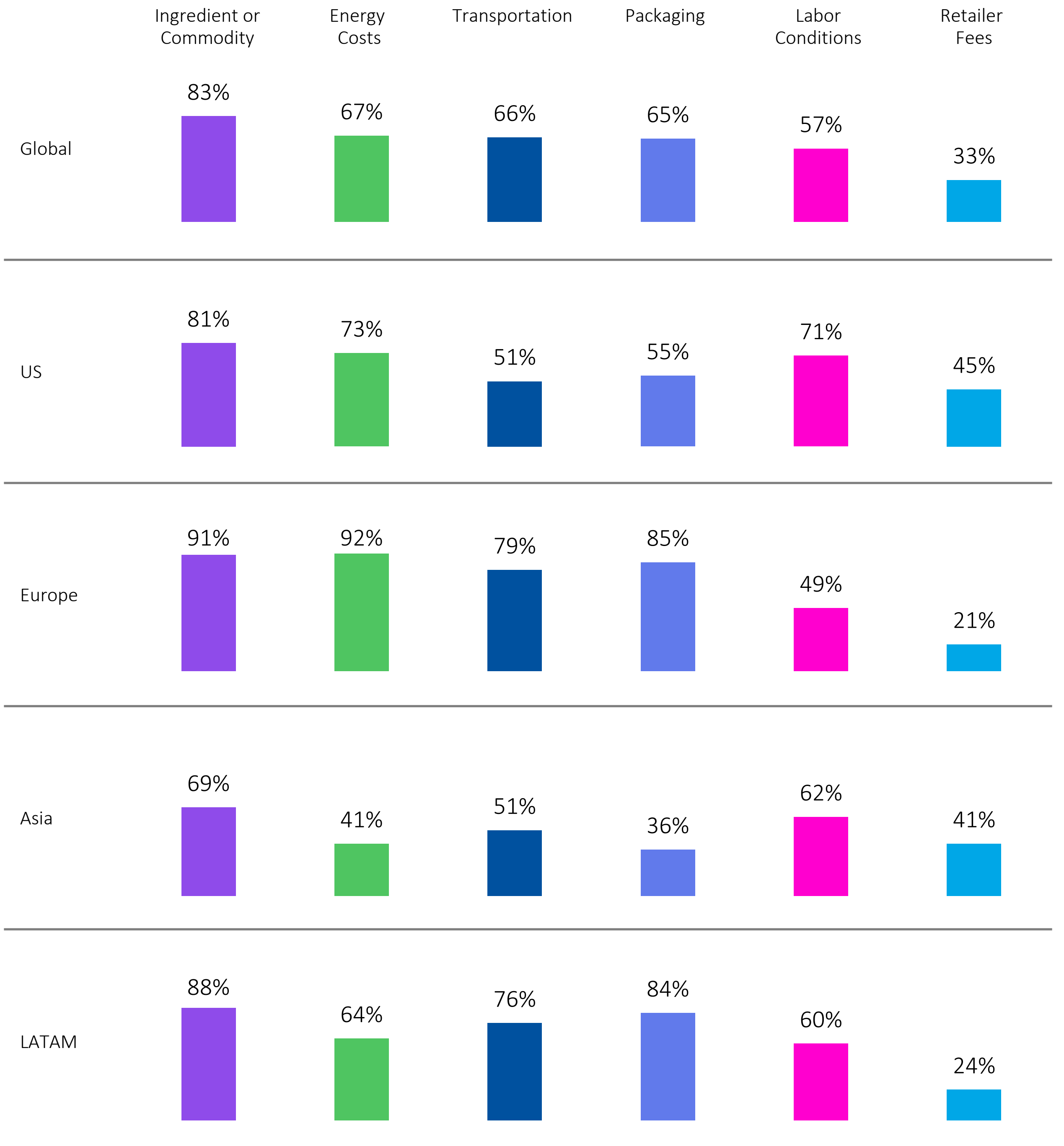


In regional terms, Europe and LATAM stand out when it comes to ingredient/commodity, with 91% and 88% of respondents, respectively, saying that these costs are higher (by more than 11%), above the global average of 83%. The ongoing conflict in Ukraine plays a significant role in driving up these costs especially in Europe, since Ukraine is a major exporter of commodities like wheat, corn, and soybeans. As the ongoing conflict in the region has disrupted agricultural production and export capabilities, reduced supply and higher prices were observed. As Europe relies heavily on imports from Ukraine, as well as from Russia and other countries impacted by the tensions in the Black Sea, the instability in the region has had a direct impact on ingredient/commodity costs in Europe.

When it comes to energy costs, Europe stands out with 93% of respondents (+26pp vs Global average) saying that these costs have increased. In fact, 73% say these costs grew higher by more than 21%. Europe's heavy reliance on energy imports, particularly natural gas, highly exposes the region to geopolitical tensions and market fluctuations. In fact, some industries are heavily reliant on natural gas as a primary source of energy, which can’t be replaced by alternative sources of energy, meaning that any disruption in this sector has a ripple effect across the region. In addition to political uncertainties and supply disruptions, Europe's strong commitment to diversifying its energy sources away from fossil fuels has also added to the rising costs in this transitional phase.

Transportation costs are directly impacted by rising energy prices. However, these costs might not have risen as much in certain regions. In the US and Asia, 51% of respondents say that transportation costs increased by more than 11% in the last 12 months (-15 pp vs Global average). It is known that these two regions have well-developed transportation infrastructure and favorable geographic proximity to suppliers and key markets, which can reduce transportation distances and costs. Even though transportation costs might have increased to a lesser extent in these regions compared to the global average, rising energy prices, changes in transportation regulations, and other factors might still contribute to increased transportation expenses for these manufacturers.

Proportion indicating cost increases in the last 12 months by region



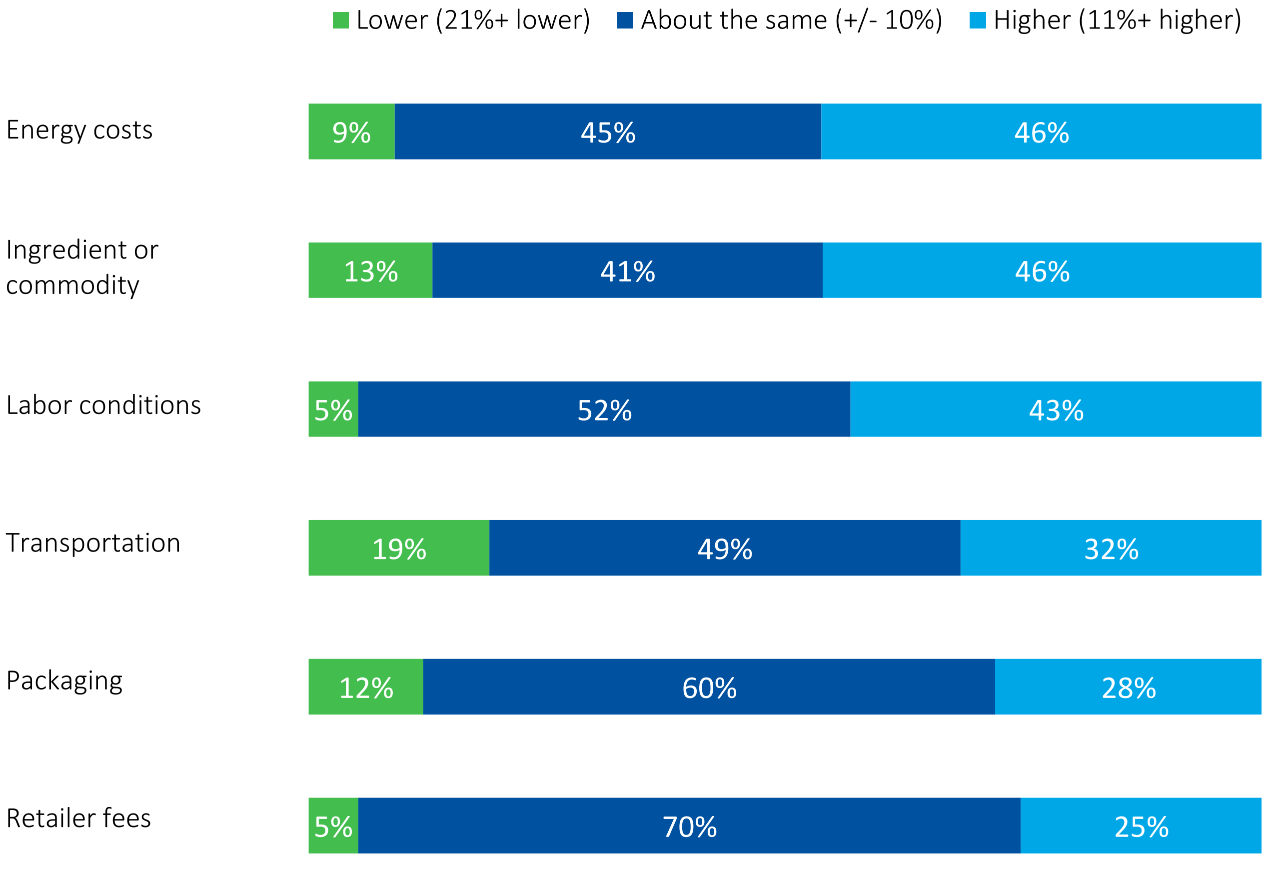
As one of the fastest growing costs for manufacturers, ingredient/commodity stands out as the number one cost driver globally. Labor conditions stand out in the US and Asia; energy costs in Europe and packaging in LATAM.

Proportion selecting each cost as the most impactful in the last 12 months

Looking forward, global inflation is estimated to slowly fall from 8.7% in 2022 to 7% in 2023 on the back of lower costs. With the global economic recovery becoming more stable, with a steady growth estimated at 3% in 2023, the manufacturing sector is expected to grow when compared to the previous year.

In the next 12 months, most costs are expected to slow down in the face of slowing demand globally, but a slight increase in supply means that prices might remain somewhat high in level terms. While half of respondents expect the cost of ingredient/commodity and energy to increase, most say the remaining costs such as labor conditions (52%), transportation (49%), packaging (60%) and retailer fees (70%) will remain about the same.

Global cost expectations in the next 12 months

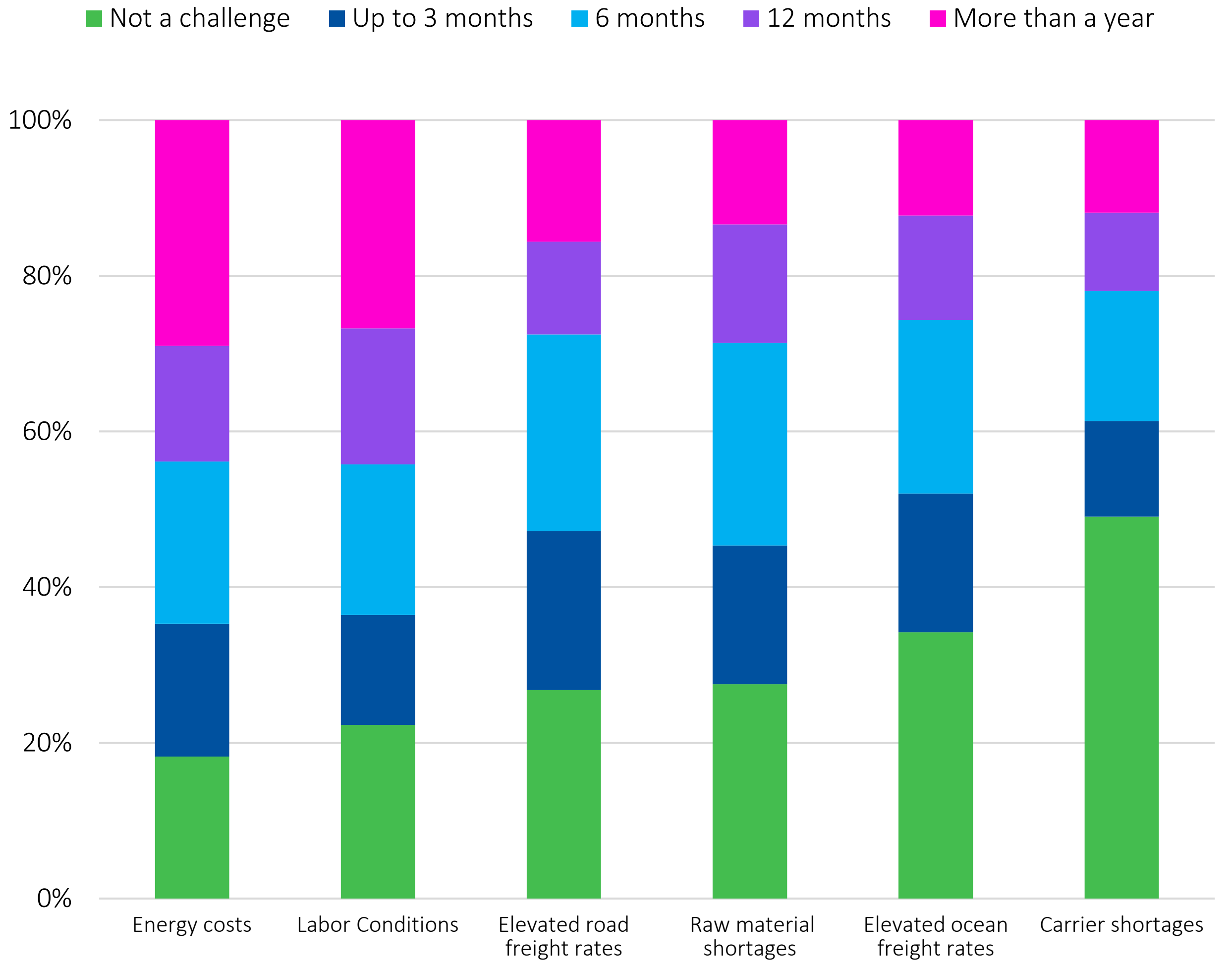


Supply chain

The challenges that lie ahead for manufacturers in their supply chains are diverse and complex. Several key challenges are expected to shape the manufacturing sector and pose significant hurdles for supply chain in the future, as we will see in more detail in this section.

Globally, more than 40% of respondents say that energy costs and labor conditions are likely to be a challenge in the long term. On the other hand, more than 30% of respondents do not consider elevated ocean freight rates and carrier shortage to be a challenge (34% and 49% respectively).

Global perceived duration of challenges



In regional terms, labor conditions stand out in the US. The manufacturing sector has dealt with worsening labor conditions since the beginning of COVID and, over the last 12 months, 71% of US respondents say Labor costs are somewhat or much higher than they were the year before. Labor conditions in the US have been a major cost driver for manufacturers and will continue to be an obstacle for the manufacturing community moving forward as 45% of respondents expect costs to continue to rise in the next 12 months.

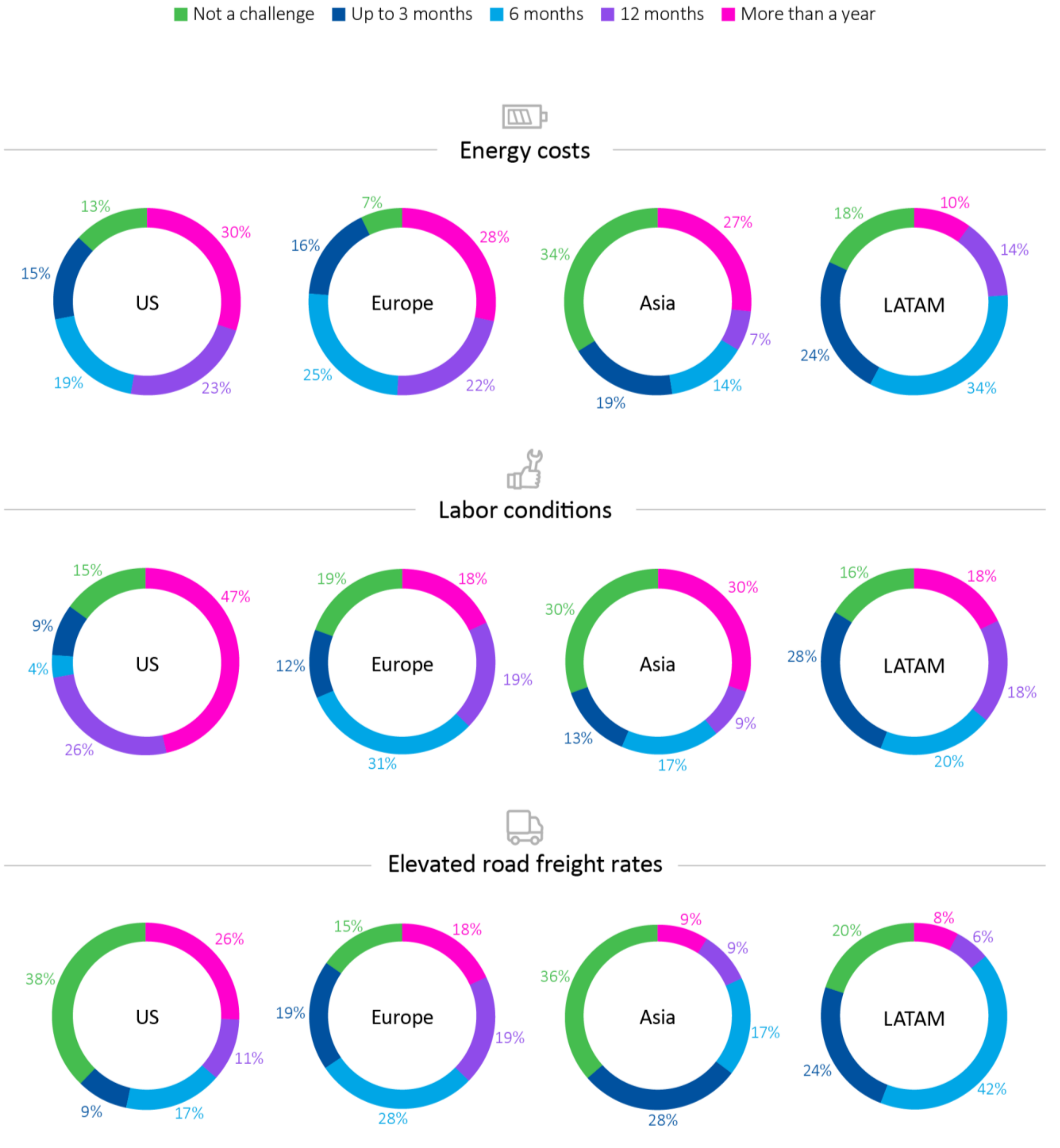
Elevated ocean freight rates and carrier shortage are not considered as much of a challenge, especially for most respondents in the US and Asia. This is more likely to be the case in these regions as many of these manufacturers are usually located near major shipping hubs and ports. This proximity can provide certain advantages, including more frequent and readily available shipping options, which may mitigate the impact of carrier shortages to some extent.

In addition, Asia and the US are naturally more self-sufficient and less dependent on imports of raw materials or energy, relying less on overseas transport and shipping conditions. Also, while the US and Asia rely more on regional trading fluxes, Europe and LATAM rely more on inbound trade.

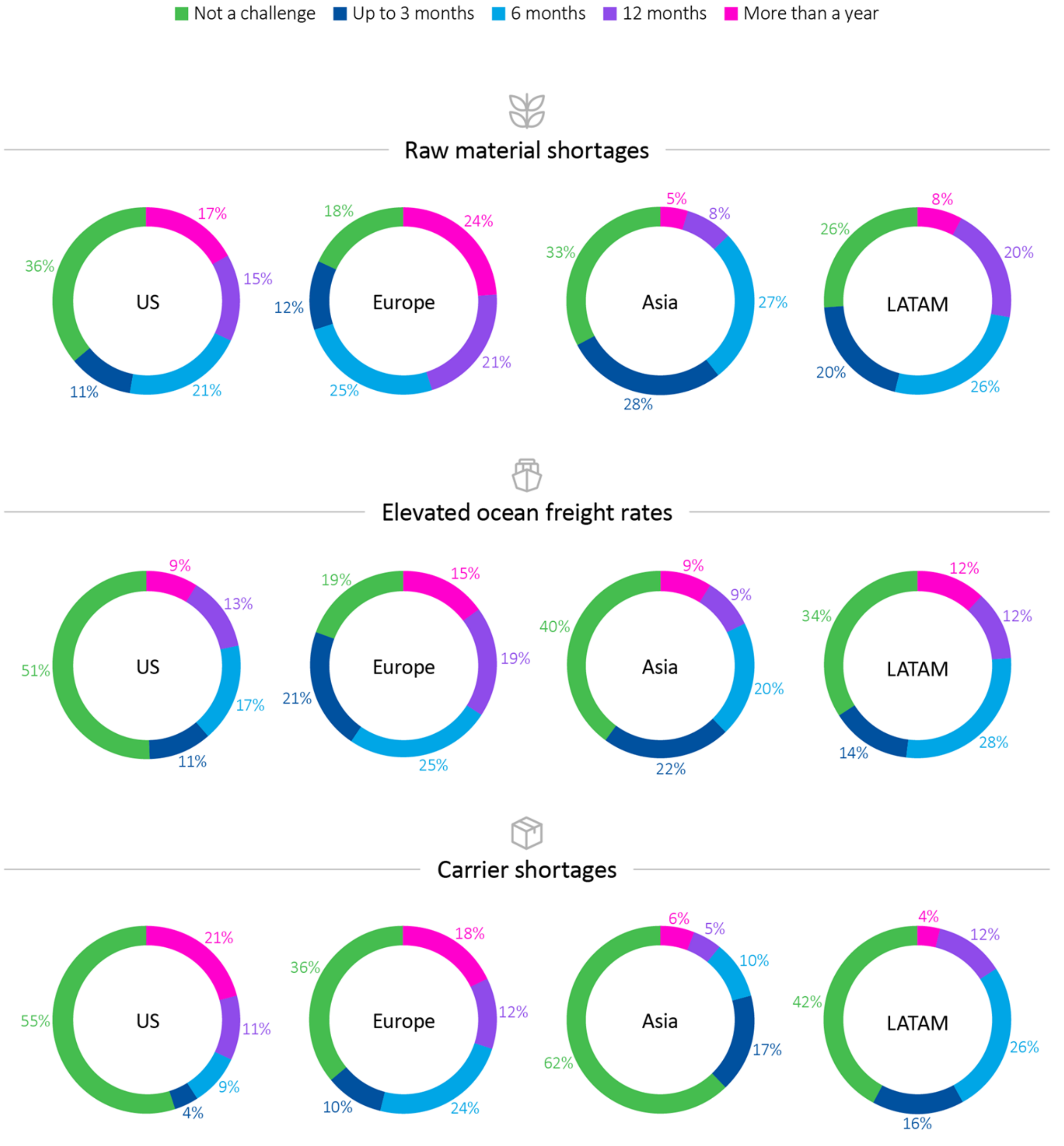
"When faced with carrier delays, Asian manufacturers frequently have access to a wide variety of shipping options, which gives them more freedom to select alternative shipping methods."

Alex Reuts, Senior Business Director, Asia

Perceived duration of challenges by region



Perceived duration of challenges by region



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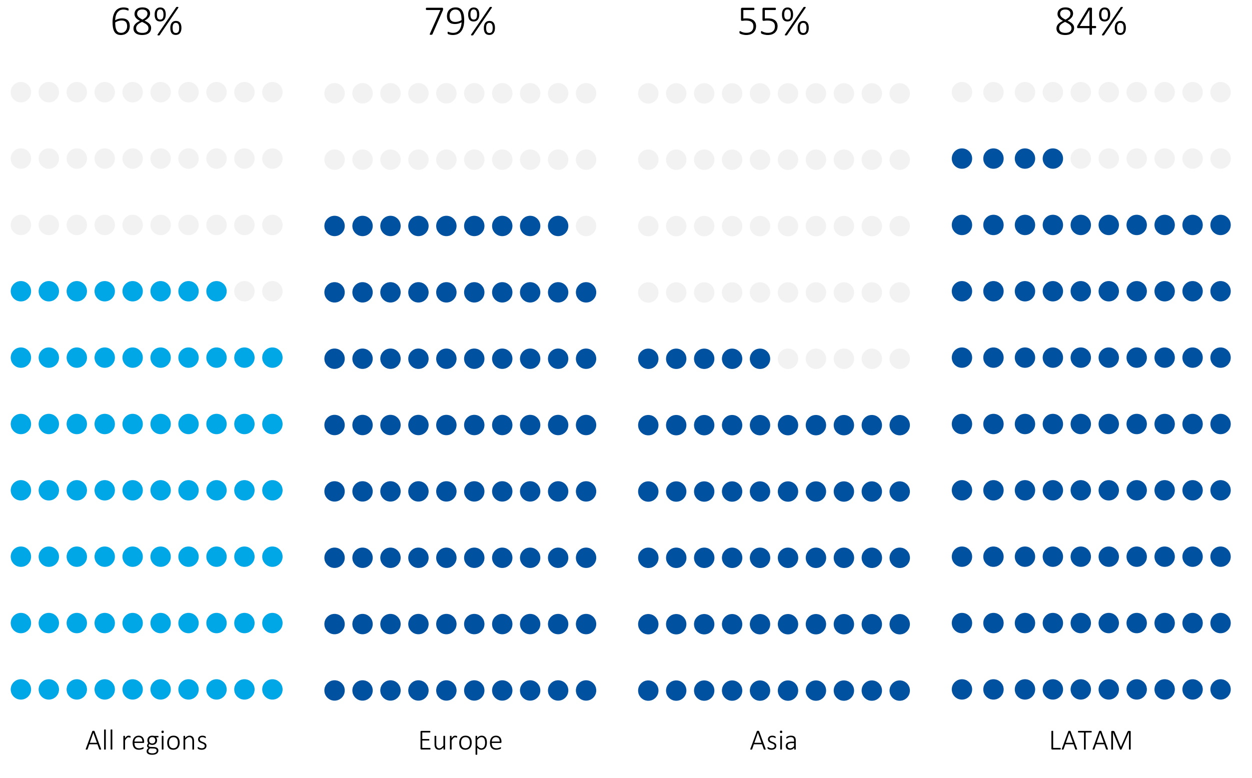
International Sourcing

This analysis excludes the US.

Trade barriers, tariffs, geopolitical tensions, or disruptions in global supply chains may drive uncertainty and potential risks to the manufacturing business. Despite most manufacturers globally (84%) being somewhat or very concerned about international trade, 68% expect to increase exports of finished goods in the next 12 months, especially in Europe and LATAM
(79% and 84% respectively).

Expectations of exporting more finished goods in the next 12 months



"Manufacturers may be actively seeking to diversify their customer base or take advantage of specific exporting conditions, such as emerging consumer demand or favorable trade agreements."

Pedro Carmo, Global Sourcing & Procurement Director (Daymon International), Global

ZOOM IN

International Sourcing

This analysis excludes the US.

More than 45% plan to import more ingredients and packaging, which may suggest a strategic move towards internal production expansion. This is more likely to be the case in Europe and LATAM.
By importing ingredients and packaging, manufacturers are more in control of their internal production.

"One of the key reasons behind manufacturers' plans to import more ingredients and packaging is the pursuit of market expansion. This may indicate manufacturers' readiness to scale up their production capacity and capture additional market share."

Pedro Carmo, Global Sourcing & Procurement Director (Daymon International), Global

Expectations of importing more in the next 12 months

CHAPTER 2

Strategies to tackle the challenging environment

As the world emerges from the pandemic and geopolitical risks continue to rise, the manufacturing sector must continue to navigate in a rapidly changing global environment. The industry has shown resilience and adaptability in the face of these challenges, with many companies diversifying their supply chains and investing in new technologies and sustainability initiatives.

In this chapter, we will explore how companies in the manufacturing sector are adapting to the key market challenges.

Private Brand

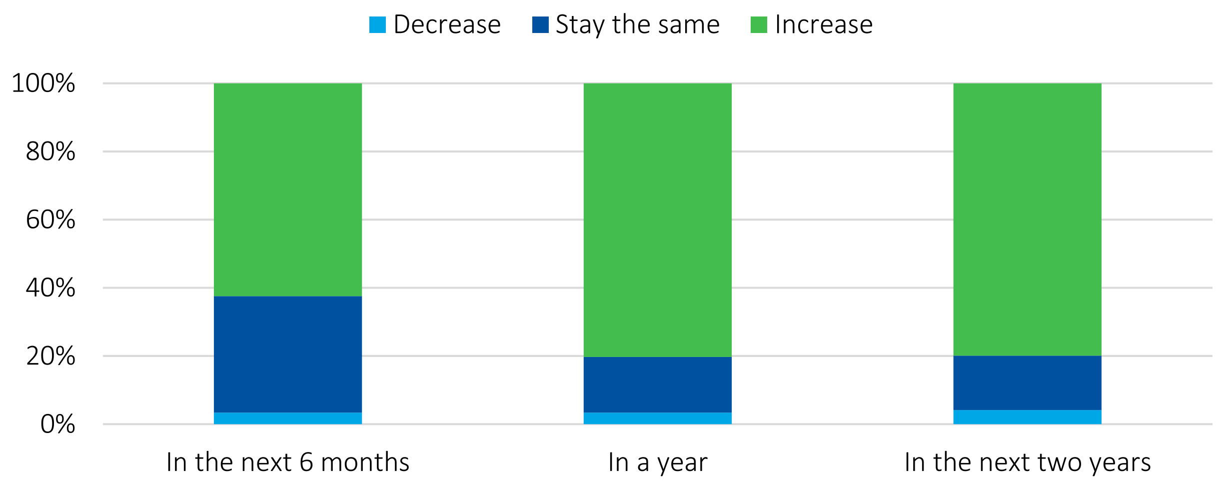
In recent years, it has become clear that inflation has been having a significant positive impact on the Private Brand business, with some of the highest inflation markets experiencing remarkable growth in their Private Brand business.

Private Brands have historically been associated with offering value-for-money alternatives to National Brands, making them particularly appealing during periods of high inflation.

Most product categories have seen significant shifts towards Private Brands, away from National Brands, which has led to an increase in the Private Brand share within those categories.

Manufacturers are increasingly optimistic about the growth of Private Brand share, with 62% expecting it to increase in the next 6 months and 80% in a year or two.

Global Private Brand share expectations for the following periods



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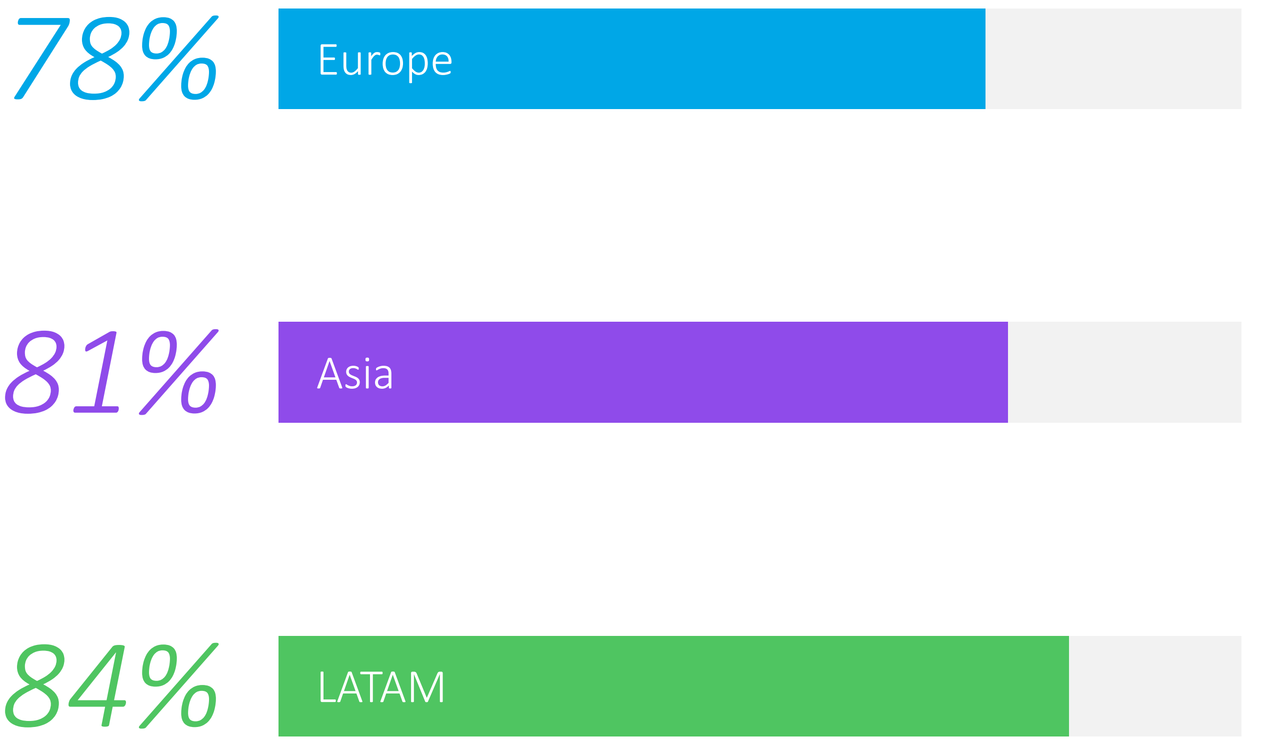
This analysis excludes the US.

Asia and LATAM stand out as regions where manufacturers' Private Brand business is expected to witness significant growth (81% and 84% respectively).

Proportion expecting their Private Brand business to increase in the next 12 months



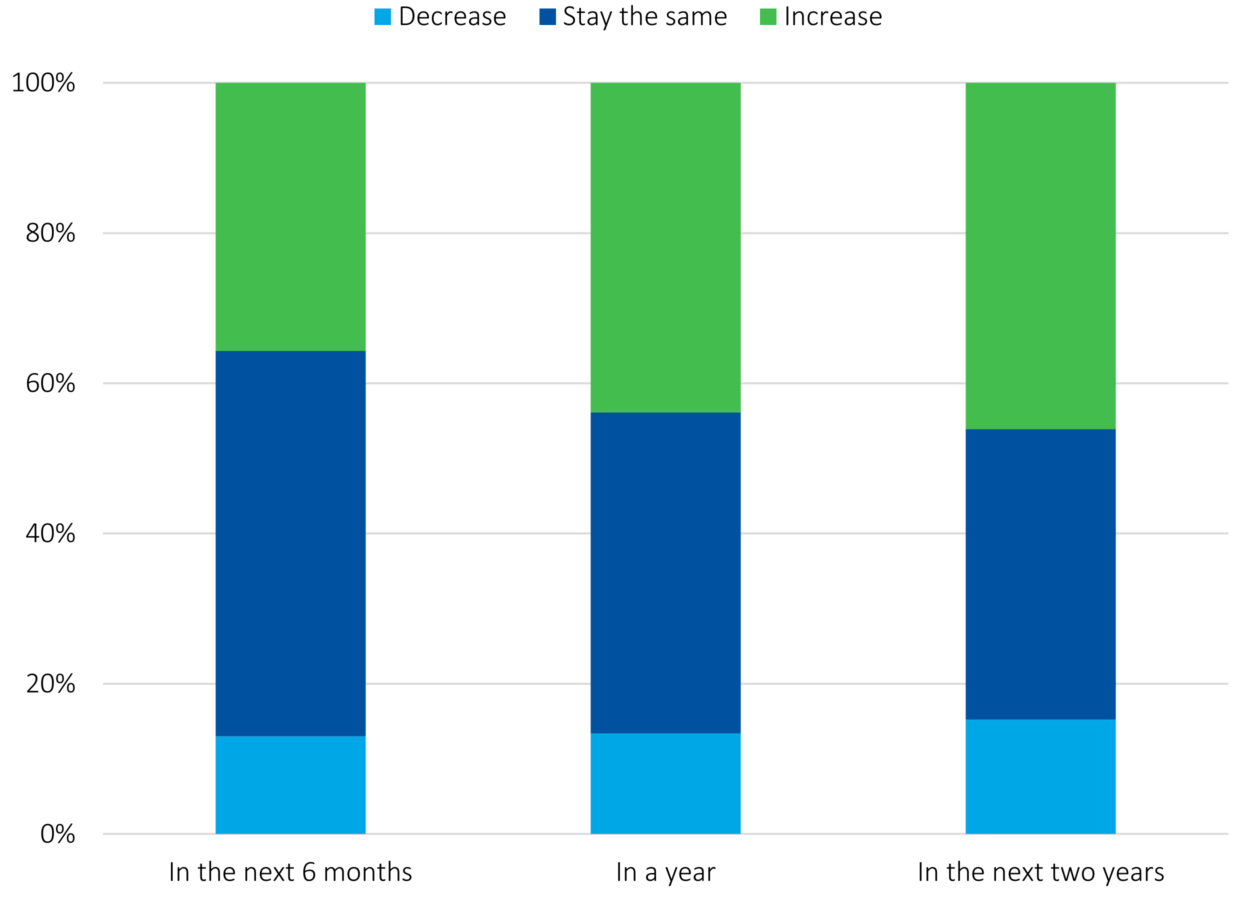
"LATAM is witnessing significant changes in its retail landscape, marked by increased retail consolidation and modernization. Large retail chains and supermarkets are gaining dominance, providing a stage for private brands to penetrate the market effectively."

Alejandro Rodriguez, Director Latin America, LATAM

In an era of economic uncertainty and rising inflation, consumers are becoming increasingly price sensitive. As National Brands face higher costs due to various factors, including raw material prices, transportation expenses and marketing expenditures, they are often compelled to pass these additional costs onto consumers. On the other hand, Private Brands have become more widely accepted and available across markets, which linked to a more compelling price positioning has led consumers to gravitate more towards these items, rather than towards National Brands.

In fact, around one in three (36%) respondents expects the price gap between National and Private Brands to increase Private Brand consumption in the next 6 months.

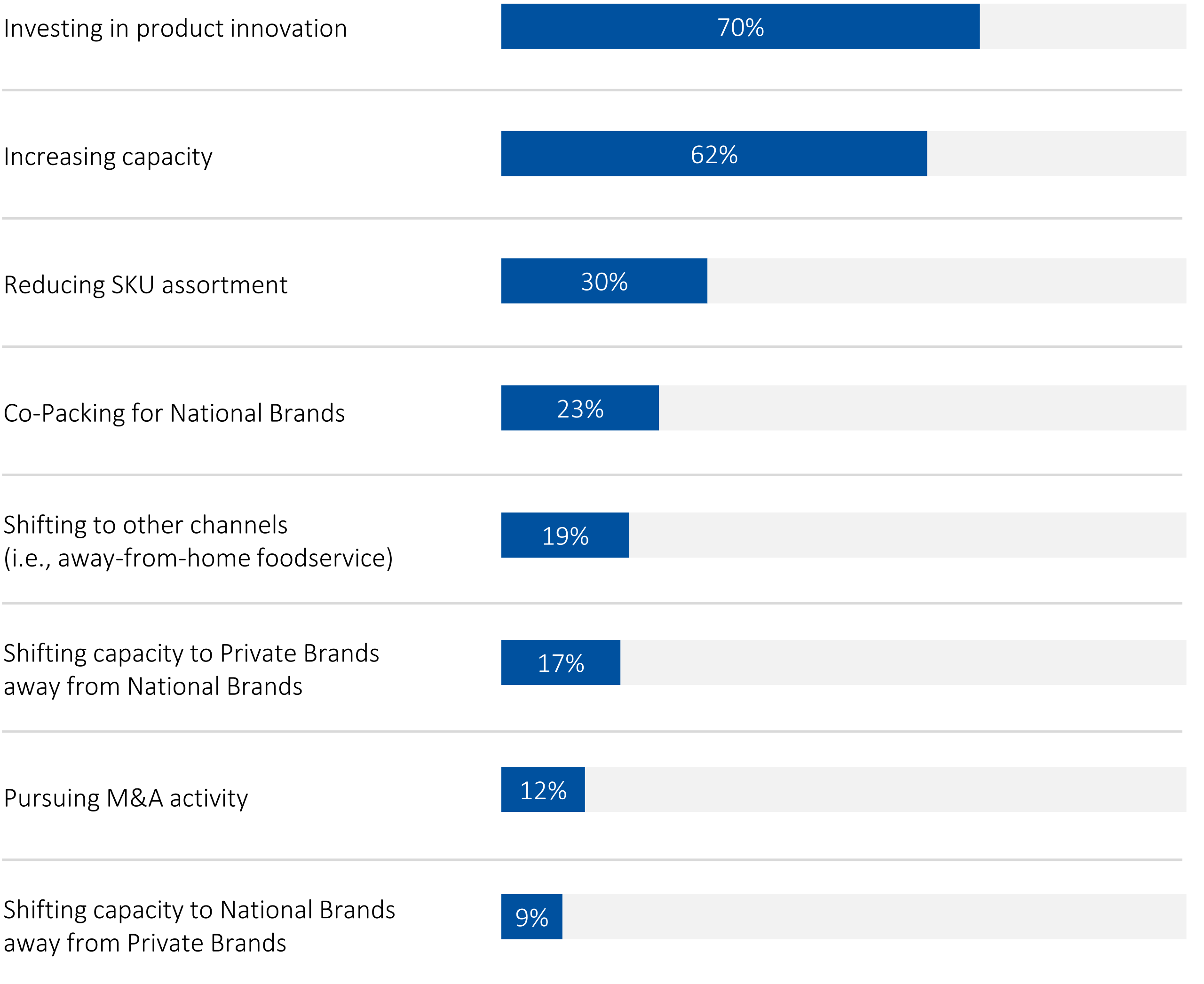
Global expectations on how the price gap between National and Private Brands will impact Private Brand consumption



In an increasingly competitive and challenging business environment, manufacturers recognize the importance of investing to remain relevant and bring differentiation to the market. Most respondents globally will invest in product innovation (70%) and in increasing capacity (62%) in the next 12 months.

Other strategies, such as reducing SKU assortment in the US or co-packaging for National Brands in Asia, are expected to be implemented regionally, although at a lower priority level.

Strategies to be implemented in the next 12 months globally



Top 4 strategies to be implemented in the next 12 months by region

Increasing capacity	79%
Investing in product innovation	74%
Reducing SKU assortment	49%
Pursuing M&A activity	38%

Investing in product innovation	67%
Increasing capacity	55%
Reducing SKU assortment	28%
Co-Packing for National Brands	21%

Investing in product innovation	71%
Increasing capacity	64%
Co-Packing for National Brands	30%
Reducing SKU assortment	17%

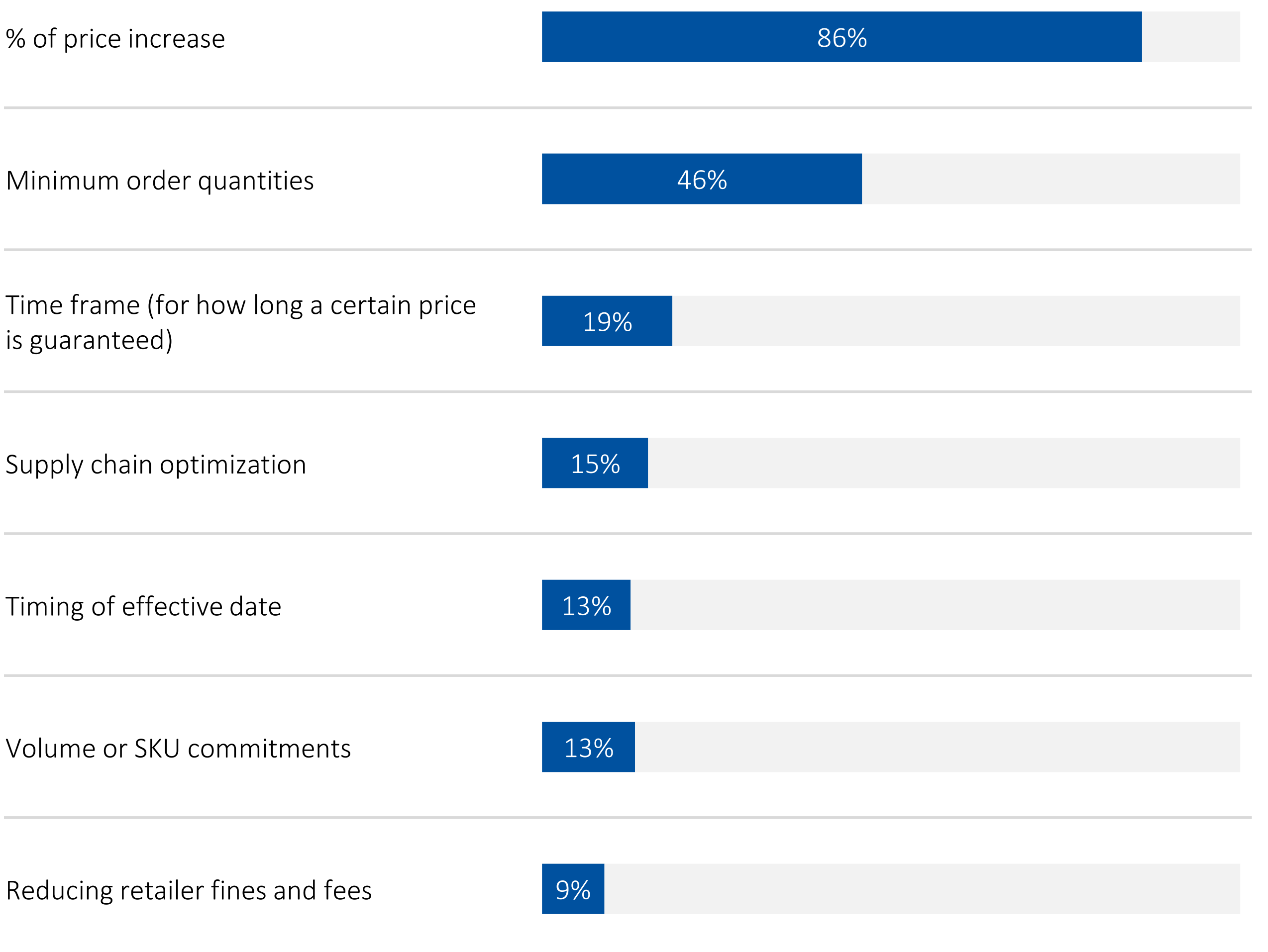
Investing in product innovation	66%
Increasing capacity	58%
Reducing SKU assortment	24%
Shifting capacity to Private Brands away from National Brands	24%

Pricing

Overall, considering manufacturers' most recent pricing action, the % of the price increase and the minimum order quantities (MOQs) are most frequently negotiated between retailers and manufacturers (86% and 46% respectively).

On the one hand, negotiating price increases helps manufacturers cover their expenses and sustain their operations, in a particularly challenging context. On the other hand, MOQs contribute to a more stable production and keep any excess inventory under control.

Matters most frequently negotiated between retailers and manufacturers during their last pricing action (globally)



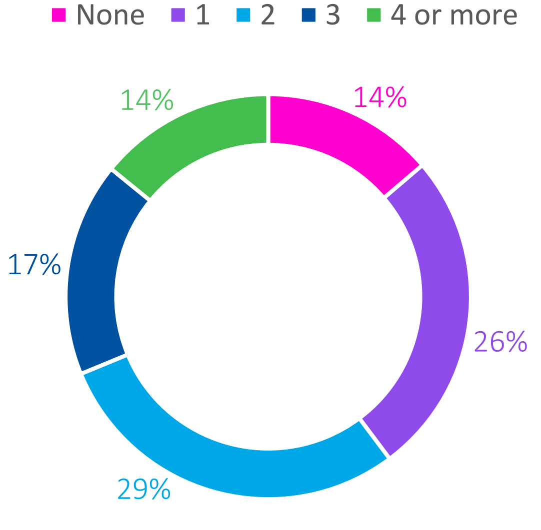
Asian manufacturers are more likely to take part in negotiations regarding MOQs than the other regions (64% vs 46% Global average).

"Asian manufacturers may prioritize long-term sustainable growth of their operations, over maintaining relationships with customers who don't contribute to the efficiency of their businesses."

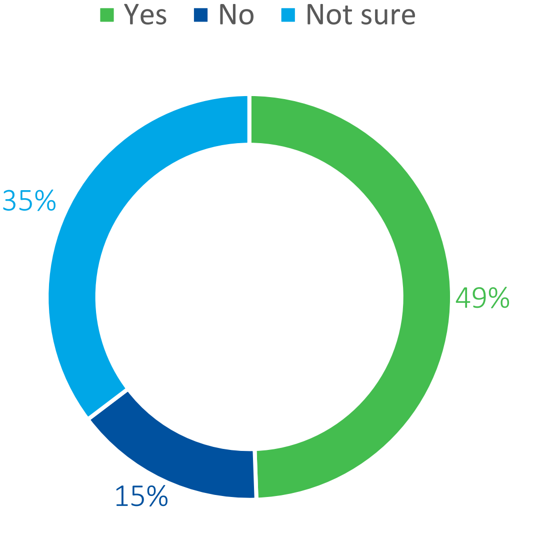
Alex Reuts, Senior Business Director, Asia

Consistent and lingering headwinds related to increasing costs may require manufacturers, in certain regions and categories, to pursue additional price increases. 60% of respondents have been compelled to implement two or more price increases in the last 12 months and 49% anticipate the need to implement additional price increases in the next 12 months.

Number of cost increases executed at a typical customer in the past 12 months globally



Global expectation of needing to pass on additional cost increases in the next 12 months



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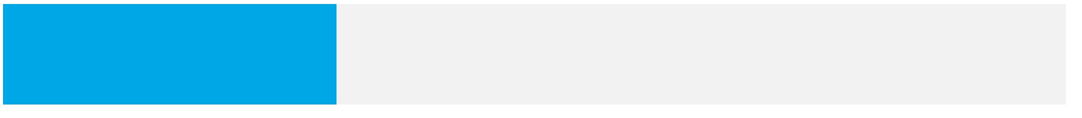
Exiting customers strategies

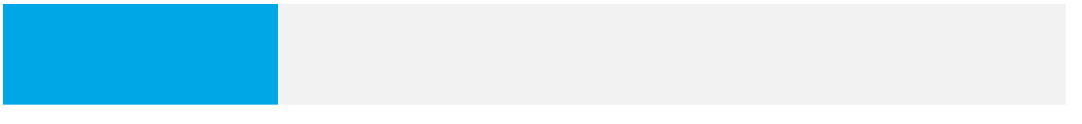
This analysis excludes the US.

In a challenging business environment, manufacturers may have to reevaluate their relationships with retail customers and may choose to exit them to maintain profitability while covering escalating costs. 32% of respondents exited retail customers by choice last year and 26% exited by raising their minimum order quantities.

32% Have exited a retail customer in full, by choice, as a way of executing a customer segmentation or rationalization strategy.



26% Have exited a retail customer in full, by choice, through raising minimum order quantities.



"By focusing on a smaller number of customers with higher order volumes, manufacturers can reduce the strain on their supply chains and maintain a more stable production flow."

Pedro Carmo, Global Sourcing & Procurement Director (Daymon International), Global

CHAPTER 3

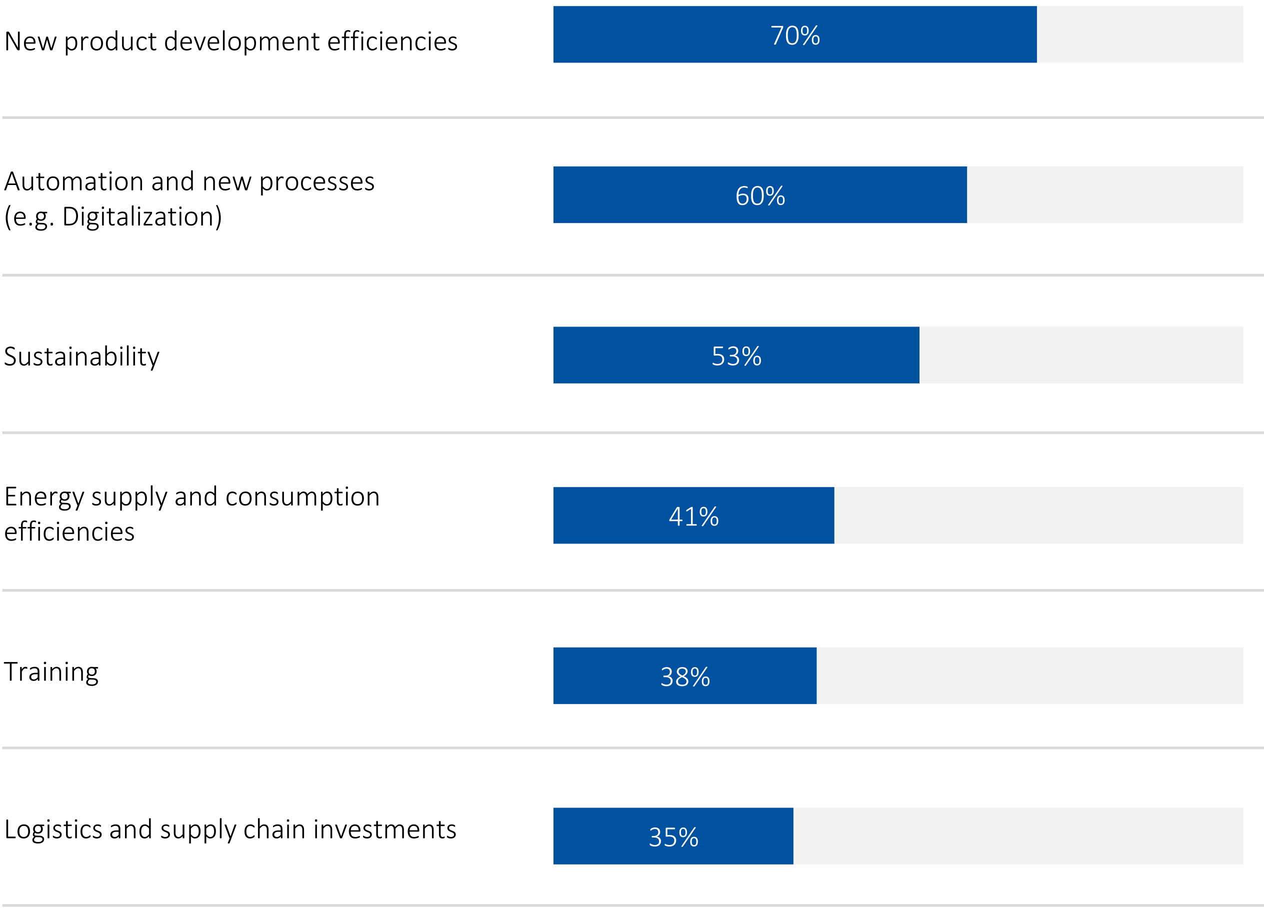
Sustainability Zoom in

This analysis excludes the US.

In recent years, the focus on sustainability has gained significant momentum across industries. Governments and regulatory entities globally have been increasingly introducing stringent environmental regulations and providing clear directions to maximize impact by 2030.
The manufacturing sector, being one of the largest contributors to greenhouse gas emissions, has recognized the urgency to address its environmental impact.

53% of respondents globally are prioritizing sustainability for investment in the next 12 months, right after new product development efficiencies (70%) and automation (60%).

Priorities for investment in the next 12 months (all regions)



Scope 3 emissions

Manufacturers have traditionally focused on reducing their direct emissions (Scope 1) and indirect emissions from purchased energy (Scope 2). However, the growing emphasis on sustainable practices has led them to turn their attention to Scope 3 emissions. By doing this, manufacturers are taking responsibility for their entire value chain and actively working towards a more sustainable future.

Scope 3 emissions usually account for more than 70% of a business's carbon footprint but are not normally reported, as current regulations are relatively loose in comparison with Scope 1 and 2 emissions. In a nutshell, the emerging Scope 3 regulations suggest that companies may have to report, relying as much as possible on high-quality emissions data provided directly by suppliers and other partners. Unlike Scope 1 and 2 emissions, which are relatively easier to quantify due to their direct (or indirect) association with owned operations, Scope 3 emissions require gathering data from multiple external sources.

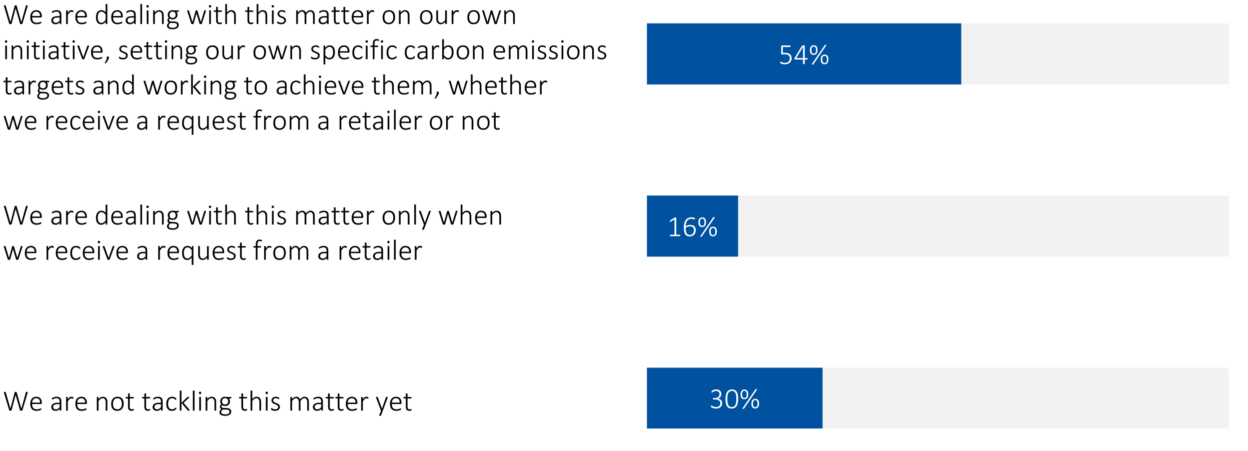
In the last decade, manufacturers have begun measuring and managing Scope 1 and 2 emissions, but Scope 3 emissions may be a more difficult task. As they navigate a changing regulatory landscape, manufacturers may also face challenges associated with data collection, supply chain engagement and implementing emission reduction initiatives across stakeholders. However, they have begun, at a slower pace, proactively tackling Scope 3 emissions reduction to ensure compliance.

Scope 3 emissions encompass all indirect emissions that occur throughout a company's value chain, including both upstream and downstream activities. They encompass emissions from sources such as purchased goods and services, transportation, waste disposal, and the use of products.

Most respondents globally (54%) are dealing with the Scope 3 carbon reduction targets on their own initiative, and working to achieve them, whether they receive a request from a retailer or not.

While manufacturers are increasingly investing in Scope 3 emissions reduction in Europe and Asia, in LATAM, 56% say that they are not tackling this matter yet.

How manufacturers are dealing with the scope 3 carbon reduction targets (all regions)



"LATAM's supply chains are often complex and fragmented, involving numerous stakeholders across multiple countries. This complexity makes it difficult to gather accurate data on emissions, trace the origin of goods, and establish transparent and sustainable practices throughout the value chain."

Alejandro Rodriguez, Director Latin America, LATAM

CHAPTER 4

Conclusions

Manufacturers have been navigating a challenging and uncertain business environment. Our 'Daymon Private Brand Manufacturer Outlook Survey 2023' has revealed that manufacturers supporting the private brand business are embracing resilience, adaptability, and forward-thinking strategies to succeed and grow.

One of the key findings of our Survey is the increasing optimism surrounding the growth of Private Brand. Across all regions, irrespective of their Private Brand maturity level - manufacturers have embraced the potential of investing in Private Brands. Findings suggest that regions where the Private Brand share has been traditionally lower than in Western countries, like LATAM and Asia, are even more likely to invest in Private Brand in the future. Still, more mature Private Brand markets, such as Europe and the US, remain optimistic and expect Private Brands to grow even further.

By focusing on Private Brands, manufacturers can flex their production, expand their reach and relevance and take advantage of the growing "consumer interest" in Private Brands.
Our research suggests that affordability may be the main catalyst for driving the transition from National to Private Brands. Indeed, faced with deteriorating economic conditions, consumers are likely to look for compromises, seeking better value-for-money products that meet their needs at a more affordable price.

The Survey also reveals that investing in product innovation and increasing capacity will be key areas for future investment.

By continuously improving and introducing innovative solutions, manufacturers will be able to overcome future challenges, such as supply chain disruptions or changing regulations, and meet customers' needs in new ways.

Moreover, increasing capacity helps manufacturers navigate unpredictable market fluctuations and sudden surges in demand. With a robust capacity, manufacturers can quickly ramp up production when needed, ensuring timely delivery and customer satisfaction. This is especially the case in the US, where there's a need to increase capacity to keep up with the current level of demand. Increasing capacity means that manufacturers can adapt their output levels more quickly to meet increased market demands or scale down production during slower periods. This flexibility allows manufacturers to maintain optimal inventory levels, avoid stockouts, and seize opportunities when market conditions improve. On the other hand, in regions like Asia, increasing Private Brand manufacturing capacity may help the region avoid an over-reliance on imports.

As manufacturers consider their priorities for the future, sustainability reaches the top three for investment, especially in Asia where environmental issues make sustainability particularly relevant. The topic is also high on the agenda in Europe, a more mature region when it comes to sustainability, although still primarily focused on recycling as a way to contribute to less wasteful packaging (as our research reveals). Although sustainability is less of a topic in other regions, like LATAM, it's likely that it will grow as a key priority in the future, in the context of the UN Sustainable Development Goals (SDGs).

In fact, Goal 12 focuses on responsible consumption and production, which relates directly to the manufacturers' business. In Europe, the European Union has published several measures on this topic, including increasing the use of recycled plastics in new products and packaging by 2025. The focus on sustainability is also likely to be pushed up on the agenda due to the consumer demand for more sustainable products and practices.

ABOUT DAYMON

Daymon is well-positioned to help businesses navigate the challenges of the current environment and identify strategies for the future. Our expertise and capabilities can provide businesses with the necessary tools to take advantage of the growth of Private Brands and enhance their market position.

Daymon's extensive market knowledge and insights encourage more informed decisions and will help businesses adapt their strategies to the evolving market dynamics. Daymon's expertise in new product development and innovation can support businesses in the creation of compelling Private Brand offerings that meet the changing needs and preferences of their customers. Daymon's global network of retailers and industry partners can open doors to new market opportunities and distribution channels, enabling manufacturers and retailers to expand their reach, and drive sustainable growth.

Daymon

With more than 50 years of experience building successful Private Brand programs around the world, Daymon has developed a unique, industry-leading approach to driving sales and profits for partners. We are the only solution provider that influences all aspects of brand development, from strategy through execution to consumer engagement. Our unique approach and proprietary methodologies help retailers and brands set themselves apart — boosting brand presence, category effectiveness and speed to shelf.

Find out more at: **idc@daymon.com**