BORD BIA
IRISH FOOD BOARD

Bord Bia's
Brexit Action Plan 2021

Financial Resilience

GETTING IRELAND BREXIT READY

7TH EDITION: MARCH 2021

Rialtas na hÉireann
Government of Ireland

SUMMARY OF ACTIONS

1. Understand the impact of your currency exposures
2. Implement plans to mitigate your currency exposure
3. Develop a hedging strategy
4. Reduce business costs in respect of financial management

Financial Resilience

This focuses on key actions Irish food and drink manufacturers can take to improve financial resilience against the uncertainties of trade with the UK under the EU-UK Trade Cooperation Agreement (TCA).

It looks at understanding the impact of currency exposures, hedging and cost reduction.

Understanding impact of currency exposures

Now that the UK is no longer a part of the EU, there is an ambition within the Irish food and drink sector to grow in other non-UK markets. There is a need to manage FX in this context as there may be fluctuations in the currency exchange rate volatility between different currencies depending on the market.
It is important that you re-evaluate the FX risk on your business.

The 2020 Readiness Radar reveals a slight decrease in the number of businesses with a formal currency hedging strategy, down to 55% in 2020, from 64% in 2019. This is likely down to the high proportion of small businesses that engaged with the Readiness Radar. In the same way that those businesses with a turnover of <€1M had less of an exposure to currency fluctuation, it is also the case that this cohort were much more likely not to have a formal strategy; with over 66% stating they did not have one, and only 11% stating they have a formal strategy with their bank.

There are some actions that should be considered in respect of prospective currency exposure:

Understand the link between Foreign Exchange (FX) rates and their commercial impact:

- What does the FX rate impact (e.g. setting a sales or purchase price)?
- Do you have the correct rate when setting the contract price?
- How will the pricing be communicated to the company’s finance function who may want to hedge the FX risk?

Engage the sales/procurement function in the management of FX risk. The function needs to understand:

- What role they need to play.
- What information they should provide and when (e.g. updated UK sales forecasts at the end of each month).
- The impact of good and bad communication of FX exposures and associated risk management on the financial results of the company.

Mitigate Currency Exposure

To mitigate currency exposure, it is important to measure the potential financial consequences of:

- the impact of a currency fluctuations on your cross-border transactions
- the impact that price inflation and tariff changes will have on your cost base and ability to mitigate exposure
- the impact of import VAT on your cash flow
- the slowed production impact on stock and sales, caused by tariff control bottlenecks

It is also important to draft and manage an FX policy. This FX policy will vary depending on a number of issues, including the types of exposures being hedged, certainty around quantum and timing of exposures, the ability to pass on adverse FX movements along the supply chain and the company's appetite for risk.

Dual Invoicing

Dual Invoicing can help you manage currency risk if you are getting two different prices in two different currencies e.g. one in € and another in US$. Having two prices can help you determine the exchange rate differences. The benefits of dual invoicing include the following:

1. You can improve your buyer power with your suppliers if you know the right value of what you are buying from them.
2. Dual invoicing can help you minimise currency conversion costs and maximise opportunities to save.
3. Having two prices can influence your decision to make the best payment option.

/USD etc. Currency Exposures	Identify currency pairings e.g. EUR/GBP/USD etc.
Source of currency exposure	This can be sales, purchases or both.
Percentage of certainty surrounding forecasts	100% certainty makes hedging easier. 60% certainty may result in 60% of forecast amounts being hedged.
Quantum	What is total amount of currency exposure?
Exposure timeframe	6 months? 12 months?
Underlying price certainty	As the exposure is a combination of price and quantity, is the foreign currency price set in the contract or is this also a variable?
Counterparty knowledge of FX movements and implications of same	Is your counterparty aware of ability of FX movements to impact on price charged to them? Will they seek the benefit of favourable moves but resist the cost of adverse moves? Will they assume a sharing of the FX risk?
Hedging lines	Do you have sufficient hedging lines in place (for both the quantum to be hedged and the period for which hedging is desirable)?
Hedging instruments	Which instruments does the company policy permit to be used?
Authorised personnel	Who can enter into FX transactions on behalf of the com-pany?
Hedging counterparties	Who to use for the provision of currency and why?
Attitude of lenders to FX management	Does your loan agreement restrict you to using lenders only? Impact of FX on wider financial metrics (including ability to service debt)?
Intercompany loans	Who takes the currency risk when loans are in a non-local currency and who is responsible for hedging this risk?
Reporting	Types and frequency of reports to manage currency exposures on an ongoing basis.

Hedging

Currency hedging is the act of entering into a financial contract in order to protect against currency volatility and protect underlying business margins. The main benefits are protection and cash flow certainty. If a business generates revenues or costs in different currencies, it is exposed to Foreign Exchange (FX) risk whereby currency movements can affect the margin a business earns. To mitigate this, many companies choose to hedge their exposure.

Hedging can:

- Provide certainty of exchange rates.
- Act as a defence against adverse movements in foreign exchange rates.
- Help with accurate forecasting and budgeting.
- Reduce the shock and impact to business, especially where cash flow or margins are tight.
- Improve bottom line performance.

The downside of hedging is that it results in a set exchange rate over a fixed time, which reduces flexibility and negates any benefits from positive rate changes.

Hedging Definitions

- **Option Contracts**
  An option contract is the most commonly used derivative, which provides the right to buy or sell a stock at a specified price within a specific timeframe.
- **Forward contract**
  A forward contract is a customisable agreement between two parties to buy or sell an asset at a specified price on a set future date.
- **Spot Transaction**
  A spot transaction is the sale or purchase of a foreign currency, financial instrument or commodity for instant delivery on a specified spot date. Usually the payment is made within one or two days of the currency, financial instrument or commodity being delivered.
- **Natural Hedging**
  A natural hedge is the reduction in risk that can arise from an institution's normal operating procedures. Typically, a company with significant sales in one country is already holding a natural hedge on the currency risks, if this is also accompanied with expenses in that currency.

Key Tips for developing a hedging strategy

The five steps below outline the approach that should be considered when developing a hedging strategy:

- **Identify your foreign exchange exposure:** Understand the total payments costs, timeline for payments and the currency used across the business value chain.
- **Decide what outcome you want from the strategy:** There are different approaches to implement depending on the outcome to be achieved. Therefore, it is important to decide whether your sole objective is to protect yourself from currency risk or to manage the impact of currency fluctuations on your business.
- **Consider which hedging strategy is the most applicable:** It is worth considering all the hedging options. The reliable options include option contracts, forward contracts, natural hedging or spot payments.
- **Implement your hedging strategy:** It is important to seek financial advice when discussing hedging options, either from a bank or a financial advisor.
- **Monitor and review the hedging strategy:** Continued reassessment might include monthly reviews of currency market volatility.

Reducing Business costs

It is important to continuously monitor the current cost base across your business. This will ensure a clearer understanding of where potential improvements can be made. The following areas should be reviewed regularly:

- **Reserves:** Maintain reserve levels in order to ensure that if there is an unplanned use of them, they do not drop below an appropriate level.
- **Borrowing:** Reduce borrowings and reliance on funding to free up cash. Debit-to-income ratio should also be monitored.
- **Pensions:** Monitor pension costs and ensure there are no deficits.
- **Budgets:** Have a flexible budget to manage adverse situations.
- **Risk tolerance:** Understand risk tolerance, so you are aware how much your business can afford to bear.

Financial Resilience Checklist

The financial resilience checklist provides you with prioritised guidance on proactive measures to take to ensure resilience to post-Brexit and Market Diversification related risks.

	REVIEWED 'BUSINESS AS USUAL'	DRAFTED A PLAN FOR IMPROVEMENT	IMPLEMENTED CHANGE FOR POST-BREXIT PROOFING
Review current finances and identify the pinch points.			
Undertake 'what if' scenario modelling on the potential impact of currency fluctuations.			
Consider approaches to hedging that may be suitable.			
Identify mechanisms to improve financial resilience and consider the cost versus reward.			
Identify areas where there is potential for operational efficiencies.			

Financial Risk Supports

Bord Bia Supports

Bord Bia's Readiness Radar

Bord Bia launches an annual Readiness Radar, which is a risk diagnostic tool developed to assess industry thinking and performance around a number of priority risks and challenges. These include Covid-19, Brexit, Challenges to Market Diversification, Sustainability Pressures, Consumer Insights and Innovation, and Talent Management.

It enables Irish food and drink manufacturers to prioritise and assess their own company specific risks facing their businesses.

Readiness Radar Gap Analysis Report

Each client company that completed the Readiness Radar received a Gap Analysis Report. The Gap Analysis Report enables you to understand your risk exposure and level of preparedness across the six key challenges outlined in the Readiness Radar: Covid-19, Brexit, Challenges to Market Diversification, Sustainability Pressures, Consumer Insights and Innovation, and Talent Management.

Currency Risk Support - Video and Q&As

Bord Bia's video FAQ series on currency risk addresses key aspects that a business needs to consider when dealing with foreign exchange, including basic principles and requirements of currency risk management. These videos include tips on when to buy, dealing with banks, invoicing in euro or sterling and if a company needs a UK bank account. Further details are available on the Bord Bia YouTube channel.

Other State Supports

Enterprise Ireland's Evolve Strategic Planning Grant

The Be Prepared Grant offers up to €5,000 to assist in the cost of developing a strategic response to Brexit. The grant is intended to provide support to clients to use external resources to undertake a short assignment to determine how the company could respond to the threats and opportunities of Brexit. The grant can be used to cover consultant's fees, travel and expenses for both domestic and international employee travel.

More information can be found on Enterprise Ireland's website.

Enterprise Ireland Capital Investment Scheme for the Processing and Marketing of Agricultural Products

This new Capital Investment Scheme for the Processing and Marketing of Agricultural Products is an EU-approved Scheme aimed to strengthen and improve the resilience of primary food processing companies, through capital investment projects, and achieving higher value add by implementing new product and/or market diversification strategies.

The maximum aid intensity that can be granted under the Scheme is up to 30% of the eligible investment costs.

For more information, see the Enterprise Ireland website.

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