FRUITS & VEGETABLES

CURRENT TRENDS

- COVID-19 has affected produce markets, causing a peak in demand and prices at the start of the pandemic, before eventually stabilizing.
- Almond crops were volatile causing prices to drop in 2020 despite record crop levels.
- Wildfires and smoke damaged California grape crops in early 2020 and the ensuing COVID-19 pandemic had a major impact on the industry.
- The Consumer Price Index for fruits and vegetables was up 3.2% year over year for December 2020 on a seasonally adjusted basis, indicating increased prices for consumers.

PROJECTED VALUES
(12-MONTH OUTLOOK)

APPROXIMATE NET RECOVERY ON COST

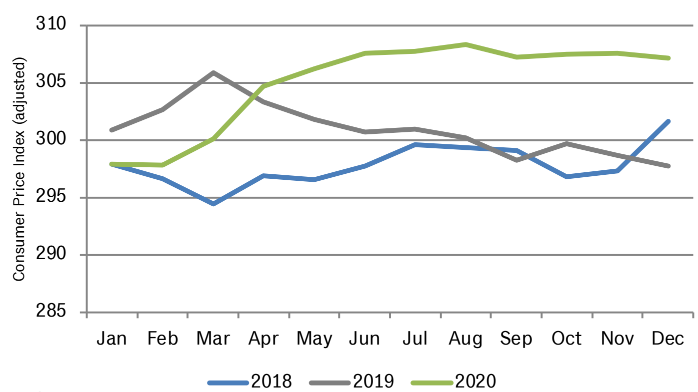
70-80%
retail packaged finished goods

65-80%
canned products

75-85%
fresh produce (net of shrink)

45-60%
bulk frozen products

CONSUMER PRICE INDEX FRESH FRUITS & VEGETABLES (SEASONALLY ADJUSTED)



Source: FRED

Gordon Brothers
1903
GORDONBROTHERS.COM
+1.617.426.3233

COVID-19 AFFECTS INDUSTRY: Global eating habits changed dramatically in March 2020 during the early stages of the ongoing COVID-19 pandemic. As bars and restaurants shut down and various states or counties went into lockdown, retailers scrambled to meet the surging demand of supermarkets and food delivery apps. COVID-19 affected much more than the end of the supply chain, as farmworkers and logistics suppliers, among others, were struggling to keep up, influencing the supply of fresh produce.

With the false belief vitamin C supplementation could help prevent COVID-19, retail demand for orange juice spiked 40% in the week ended March 14, 2020, causing orange juice futures to rocket, making the "usually sedate asset the best-performing commodity in the first quarter of 2020," according to *The Wall Street Journal*. Concerns about supply further fueled demand in early 2020 with farmworkers staying at home to avoid contagion from fellow citrus pickers, according to Jack Scoville of The PRICE Futures Group, a financial consulting firm. Traders were also pricing in expectation of a strong hurricane season, which impacted yields.

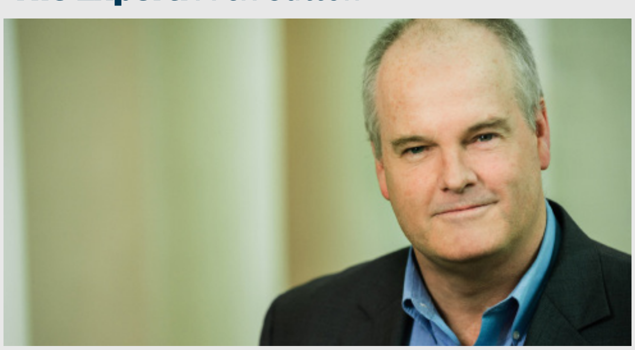
Prices were generally higher in many product segments and produce volumes were down due to the negative impact of COVID-19 on the food service industry. While some volumes were shifted from food service to the grocery segment, the overall effect resulted in lower produce volumes over the course of 2020. After demand and prices of fresh produce peaked during the first weeks of the pandemic crisis, both eventually stabilized, as overstocked consumers reduced their spending and growers felt the hit from a reduction in demand from the food service and hospitality industries. However, ongoing concerns about labor shortages hit the fresh produce industry, which runs on a strict planting, harvesting and logistical schedule that cannot always be adjusted on short notice. According to the Produce Marketing Association, sales of fresh produce increased during the initial March peak in demand by 30% to 40%, over the comparable period in 2019. The biggest increases were seen in potatoes at 114%, berries at approximately 23% and onions at 68%. Avocados saw a sharp decline in demand from food service clients, driving prices during the early shutdown period down 18% in the U.S.

The United Fresh Produce Association estimated the overall produce industry will take a $5 billion hit from the COVID-19 pandemic, although it will be some time before the full extent of its effects are known. The Consumer Price Index for fruits and vegetables was up 3.2% year over year for December 2020 on a seasonally adjusted basis, indicating increased prices for consumers.

From an inventory valuation perspective, while certain inventory positions may be impacted by short-term price fluctuations, on a mark-to-market basis recovery rates should hold up despite the impact of the COVID-19 pandemic.

CROP VOLATILITY IN ALMOND MARKET: For California's almond industry, 2020 was a bumper year bringing a record crop of 3 billion pounds; that being said prices were historically low due to the impacts of COVID-19.

The Expert: Alex Sutton



Alex Sutton provides specialized industry guidance and market research to support Gordon Brothers' Commercial and Industrial Valuation practice. Prior to this role, Alex headed Gordon Brothers' Industrial Valuation practice, where his team produced reports used primarily for financing and financial reporting. Read his full bio here.

Dutch multinational banking and financial services company Rabobank estimates that the ongoing 2020/21 crop is going to be 18% higher than the 2019/20 season production, "a milestone that was expected to be reached by 2022 or 2023," according to the bank's August 2020 Agribusiness Review.

The overall almond supply was up nearly 40%, boosted by a significant carryover from the prior season, according to the August 2020 industry position report from the Almond Board of California. The 2020 bumper crop drove prices down significantly, and it is anticipated crop levels will remain consistent for the next few years. For a portion of 2020, prices stood at about $1.40 per pound, which was below the cost of production for many growers, and down approximately $1.00 per pound from 2019.

The coronavirus pandemic had a significant effect on the overall marketplace in 2020. Supply chain disruptions slowed export sales for almonds during the early months of the year, which caused prices to fall as overseas markets accounted for 67% of U.S. almond shipments, according to information published by Rabobank for the 2019/20 season. The slowdown was especially notable in India, the industry's largest export customer.

Lenders should be aware that market pricing for crops like almonds are volatile and can change quickly, especially during a harvest period. Additionally, crops on hand from the prior year can lose value when a bumper crop harvest is ongoing and driving down market prices.

WILDFIRES DAMAGE CALIFORNIA GRAPE CROPS: At the outset of 2020 an overstock of grapes put pressure on the price of wine, and the ensuing COVID-19 pandemic hit wine sales to restaurants and hospitality venues significantly. A wildfire in Northern California, named the Glass Fire by dispatchers after a nearby Glass Mountain Road, started on September 27 and was active for 23 days. The fire damaged or destroyed property at more than a dozen wineries in Napa and Sonoma, and countless acres of grapes faced the possibility of smoke damage. Even if vineyards did not burn during the fires, "smoke taint," as it is called in the industry, can ruin wine and prevent winemakers from purchasing crops during a harvest.

President of the California Association of Winegrape Growers John Aguirre noted it was unfortunate that many winemakers had decided not to take grapes because it puts all the liability on the growers. Grapes can be tested for smoke taint, but it can take 30 days to get results and with limited harvest timing, waiting for test results is not always possible. Many winemakers do not want to risk producing wine that is tainted and, as a result, opted not to purchase smoke taint grapes as planned.

The COVID-19 pandemic had a major impact on the industry. An analysis by the California Association of Winegrape Growers calculated the pandemic had caused $400 million in losses by the fall of 2020 for a grape crop that is usually worth $4 billion. The association estimated the Glass Fire smoke could do just as much, or even more damage.

From a valuation perspective, Gordon Brothers has seen some volatility in wine prices, but overall demand, especially on the retail and off premise sides of the business, has been strong and somewhat balanced weakness in the food service, hospitality, and on premise segments. Gordon Brothers expects a decline in recovery for wine intended for the food service segment and an improvement or stability in retail product going forward.

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