Buyer Aware Part II

The food processing industry in crisis and the effect on consumers in Canada

Basic Facts

- The food and beverage manufacturing sector is the most important market for Canadian agricultural products – accounting for almost half of it's output
- Second largest manufacturing industry in Canada accounting for 14% of all manufacturing shipments, with production worth $87.3 billion; and the largest manufacturing sector in most provinces
- Accounts for 2% of national GDP
- Largest manufacturing employer – providing employment to 296,000 Canadians. Important employer in many rural areas across Canada
- Supplies approximately 77% of all processed food and beverage products available in Canada

Industry Challenges

- In recent years, the industry has been challenged by the high Canadian dollar, rising input costs, labour shortages, and growing competition from rapidly developing food exporters such as China

- The current global economic recession and tight credit market are adding further pressures by reducing consumer demand for certain products here and abroad
(in particular, the US) and making credit more difficult to access and costly

- Industry performance in terms of the trade balance and industry output has weakened over the past two years and is the worst since the early 1990s

- This situation has led to plant closures and the loss of thousands of food manufacturing jobs in Canada

The food processing industry is rationalizing due to strong competitiveness pressures

- At least 24 significant plant closures in the past two years, a third have involved large facilities (i.e., more than 200 employees)

- In some cases this has led to the loss of buyers for Canadian agricultural producers (e.g., the closure of CanGro meant the loss of all tender fruit processing capabilities, excluding juices, in Canada)

- Although some of these closures are the result of companies centralizing operations, other companies have simply closed their Canadian operations (e.g., Hershey’s and Welch’s)

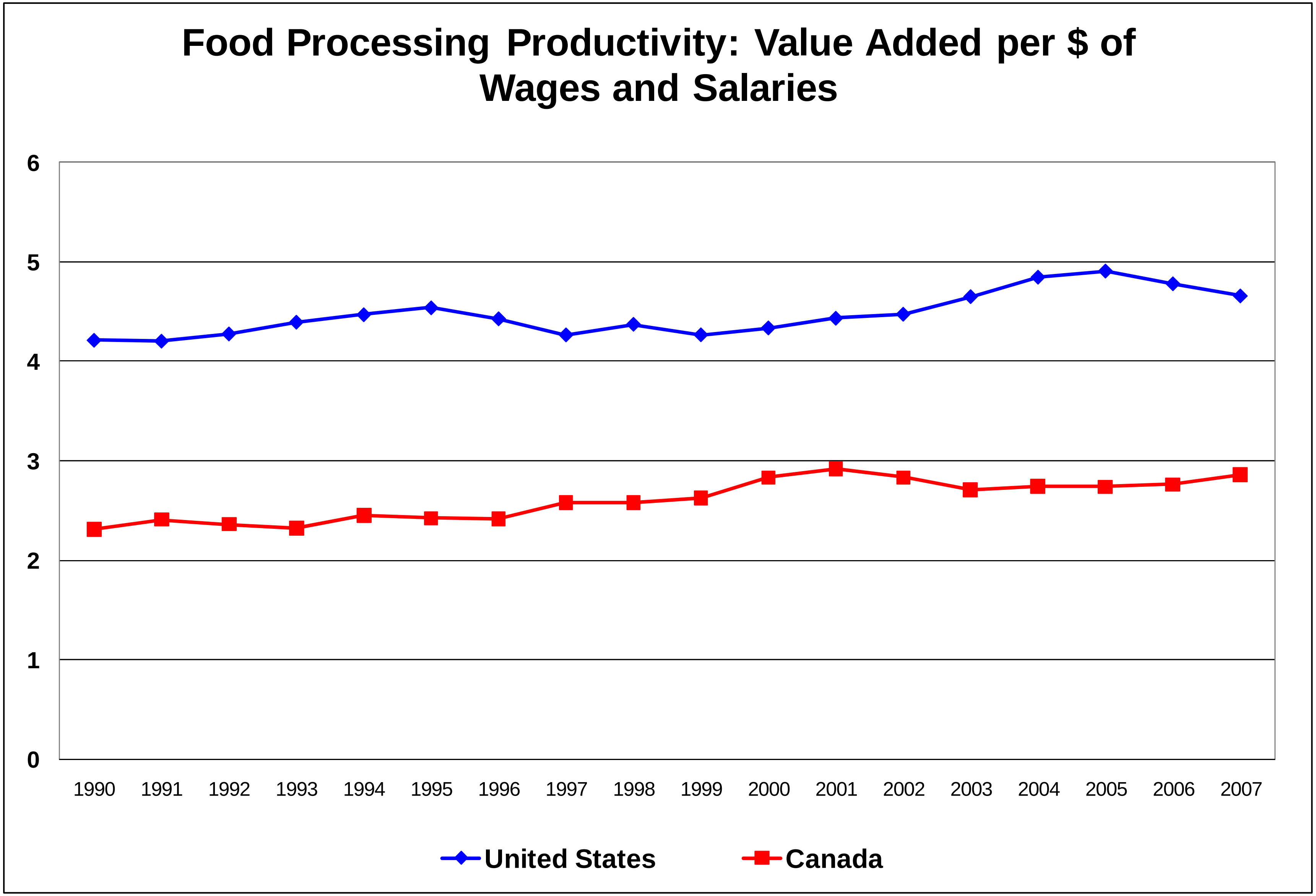
WHY ?

- George Morris Centre studies indicated that the Canadian industry is 40% less productive than the US.

- At a 70 to 80 cent rate to the US $ these deficiencies were masked but today's exchange rate has removed this crutch.

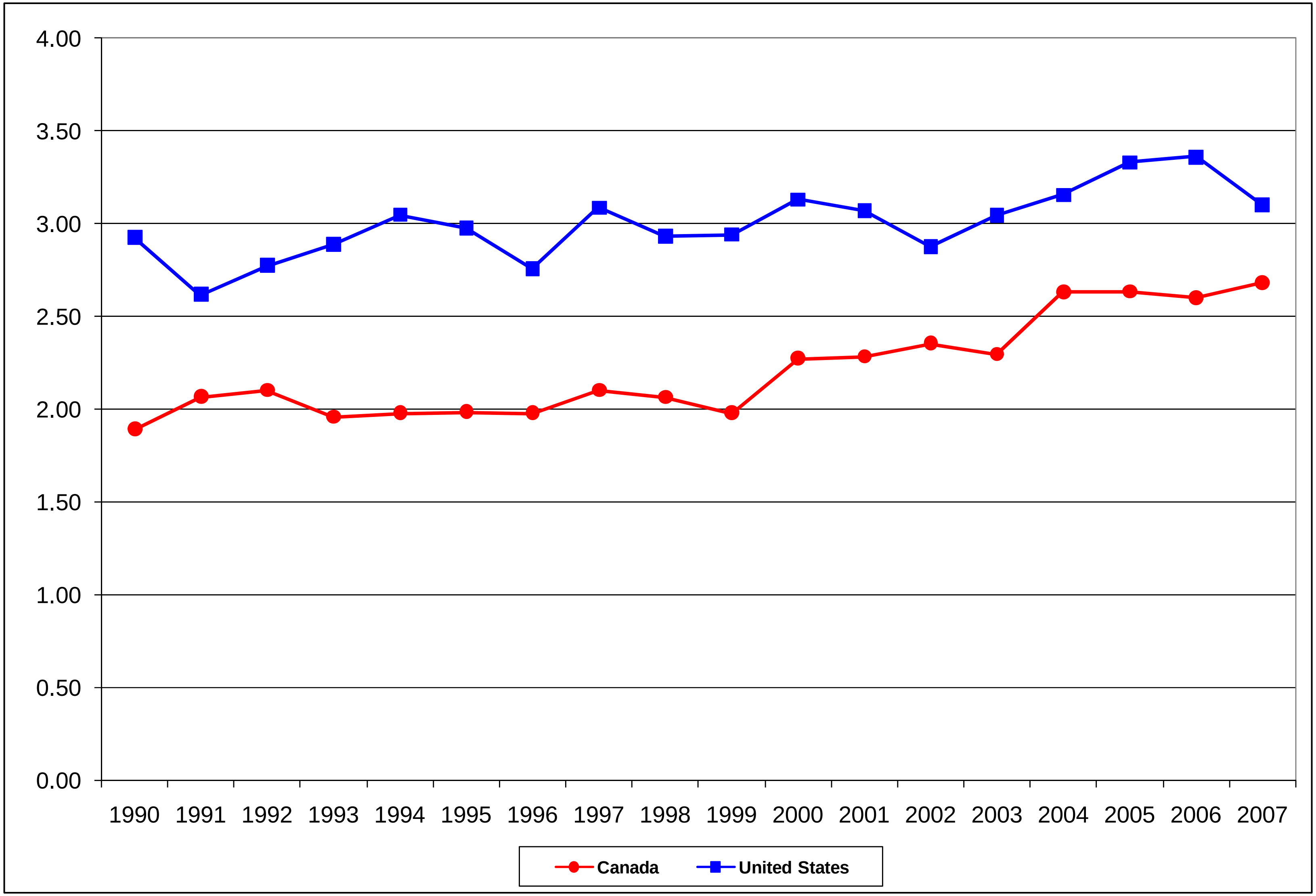
- While the US industry makes annual capital investments in excess of its depreciation the opposite is true in Canada. The industry is falling further behind in modernization with more negative implications on productivity and competitiveness and the result is clear:

WE ARE LOSING THE BATTLE

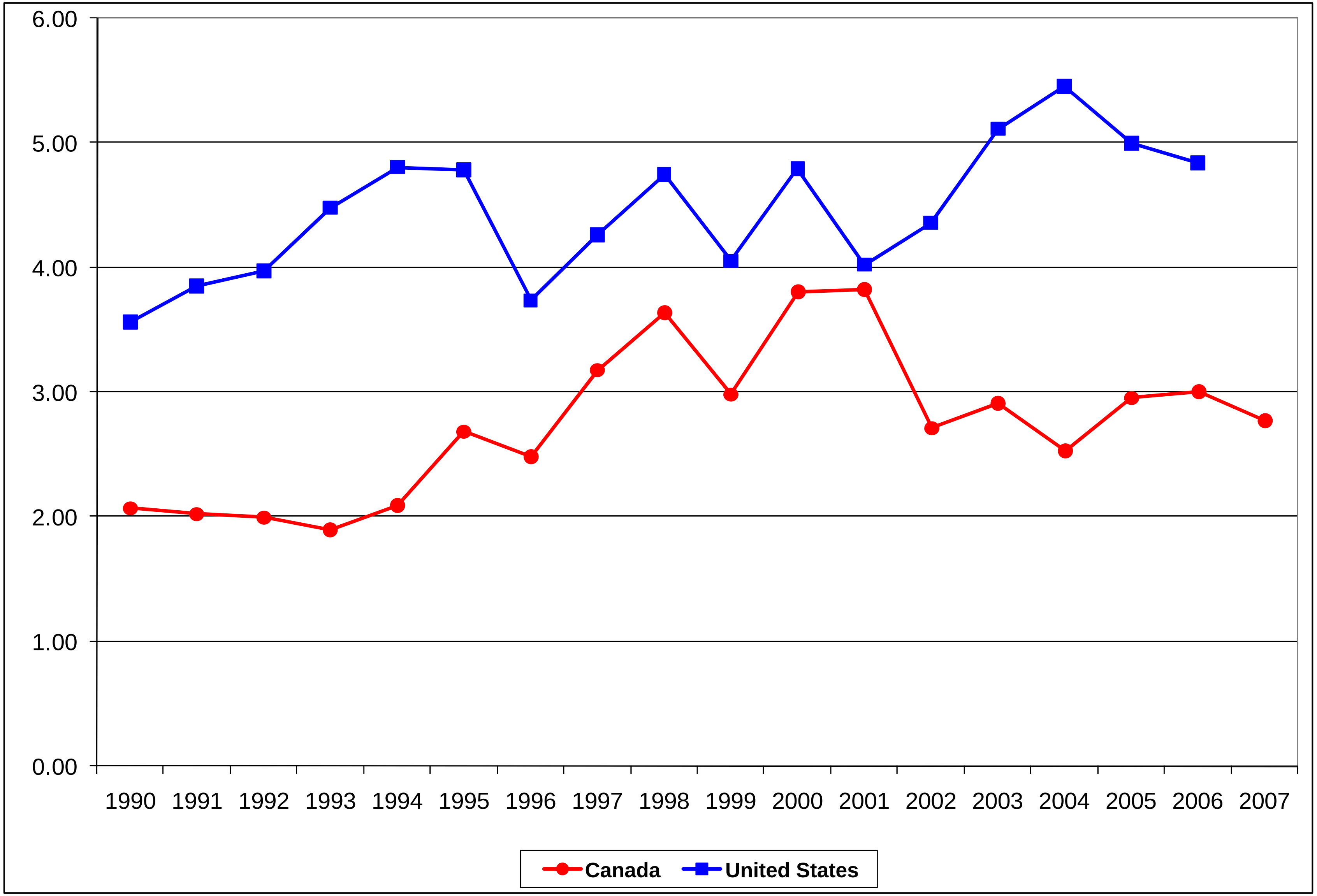


Food Processing Productivity: Value Added per $ of Wages and Salaries
6
5
4
3
2
1
0
1990
1991
1992
1993
1994
1995
1996
1997
1998
1999
2000
2001
2002
2003
2004
2005
2006
2007
United States
Canada

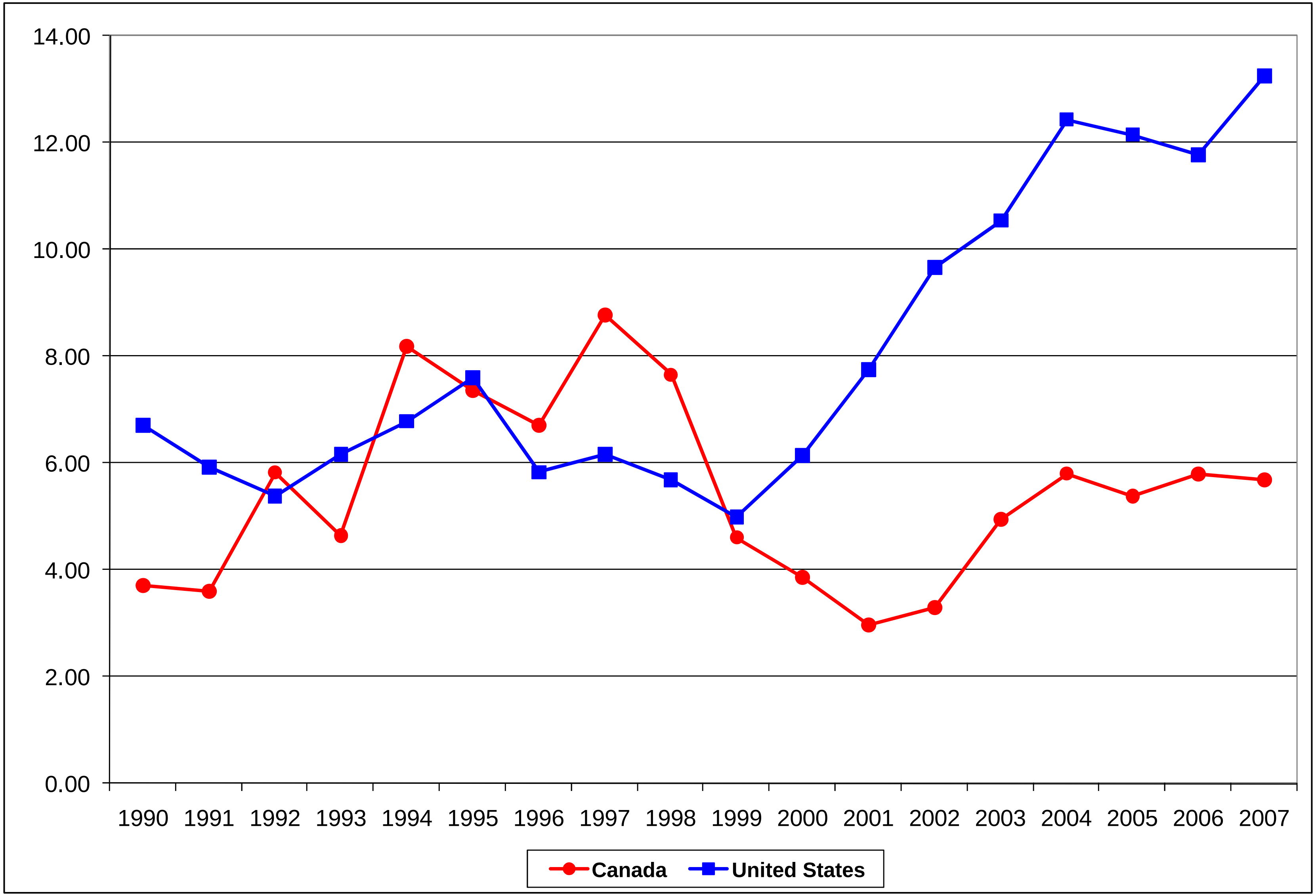
Red Meat Productivity



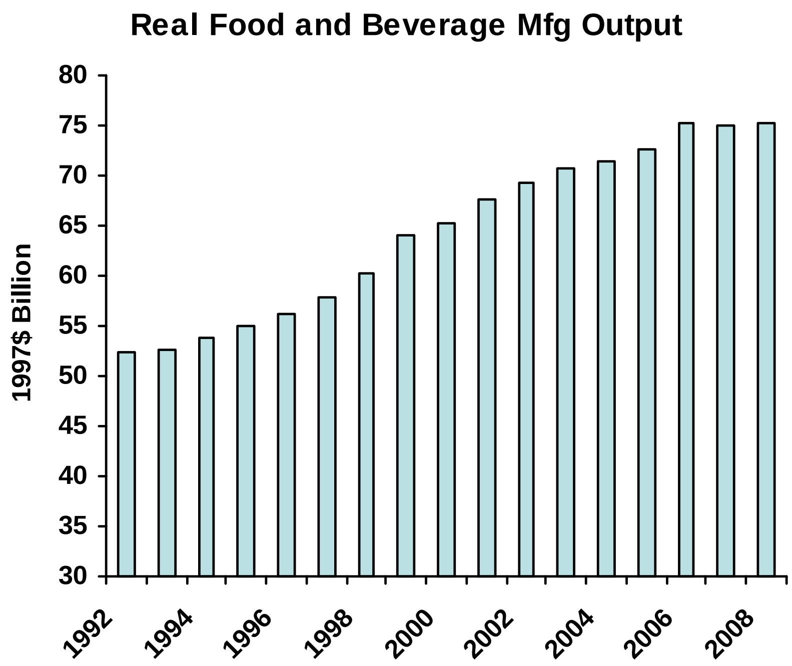
Flour Milling Productivity

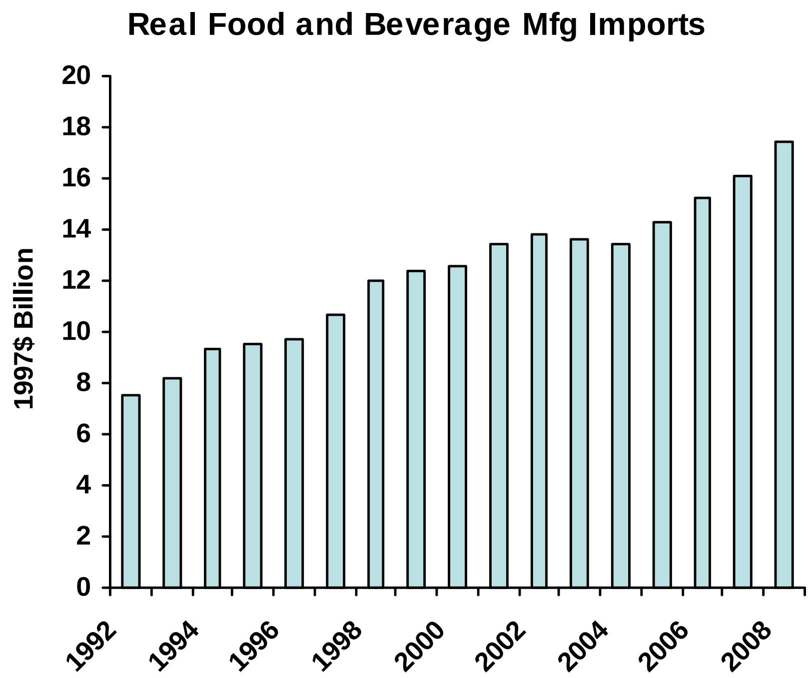


Oilseed Processing Productivity



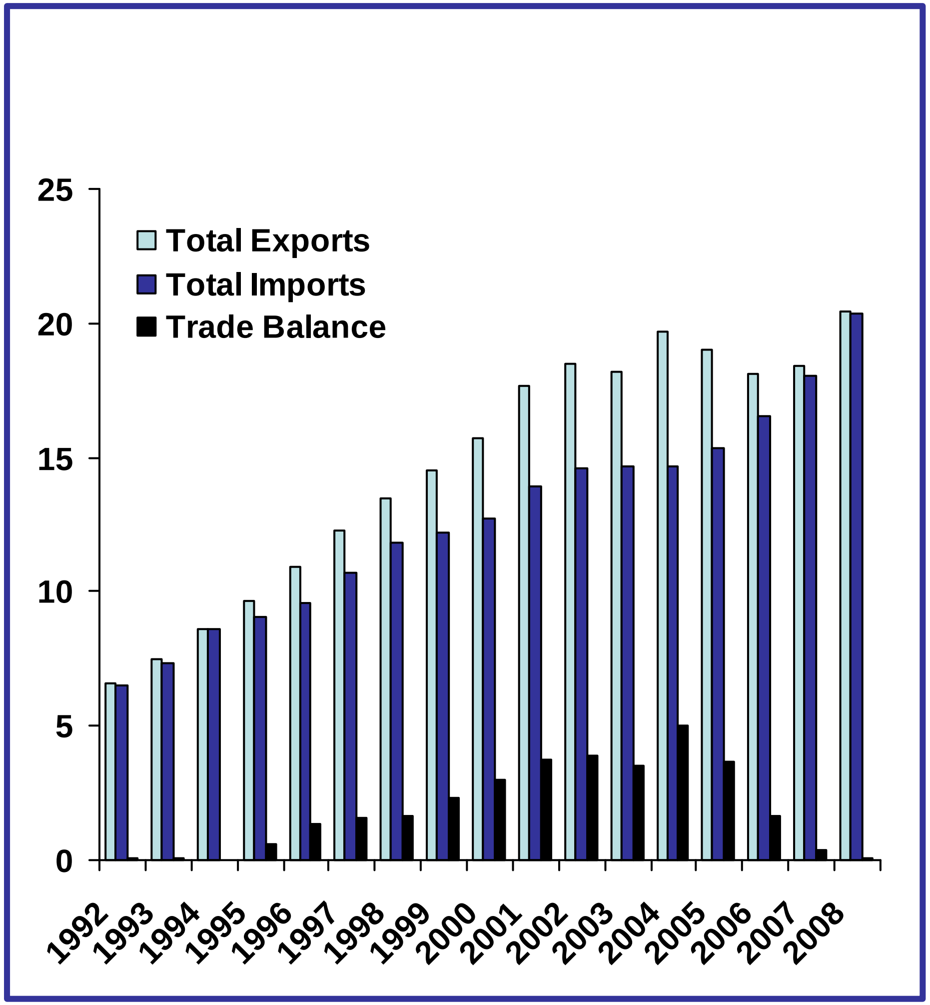
Cdn manufacturing vs imports





Canada’s food trade balance is declining

- Trade balance has been positive since 1995
- In 2004, the trade balance peaked at $5B but has declined annually since then
- In 2008, the trade balance stood at $0.1B, compared to $1.6B in 2006 – lowest level since 1994
- Weakening of the trade balance is occurring in our U.S. and off-shore markets but is somewhat worse in the U.S. due to rising $Cdn
- Trade figures for the first eight months of 2009 indicate a negative trade balance this year



Remarks by Rory McAlpine, Vice President, Government and Industry Relations - **Maple Leaf Foods Inc**

- The Harper Government seems fully aware of the need to close Canada's productivity gap with the U.S. This is strongly emphasized in their *Advantage Canada* plan, their tax cuts and fiscal policies, their investments in infrastructure and research and development, their efforts to improve Canada's regulatory framework, their appointment of a panel to review competition policy, and so on. At the provincial level we have seen governments cut or eliminate capital taxes, invest strongly in higher education and skills training and support investments in new, cleaner technologies. And yet, with all these building blocks in place, and repeated international survey's over several years that suggest Canada's investment climate is among the best in the world, we just never seem to close the productivity gap. What are governments doing wrong? What do they need to do better?

Are government actions really serving Canadian's interests in food ?

- Product of Canada requirements
- Additive & Ingredient approvals
- New Product approvals
- CFIA inspection – domestic vs import
- Labeling and Health Claims
- Access to capital
- Labour policy
- Input costs
- Support of "Buy Local"

So what does this mean to consumers ?

- At the first conference speakers identified the following consumer issues:

- **Ms. Wendy Holm P.Ag.** : “The concept of “locality” is increasingly becoming a priority for the consumer: includes production, growing, processing, storing, sourcing locally (e.g. 100 mile diet)”…… “every Canadian has the right to a secure daily supply of affordable, accessible, safe and nourishing food”

- **Dr. Ellen Goddard, University of Alberta : “**AAFC/IPSOS REID survey in 2004 found that food safety is only “top of mind” for 3% of the population” ….”AAFC/IPSOS REID survey in 2006 found an increase in confidence in food safety, and that concerns about food processing drive concerns about food safety

At the first conference speakers identified the following consumer issues:

- **Dr. Bob Church**, ***Canadian Agri-Food Policy Institute:*** "80% of coronary heart disease and stroke, and 40% of cancer, could be prevented with healthy eating (Heart and Stroke Foundation, WHO)" …" Food processors are responding: Food products launched with health messaging worldwide

- **All Speakers Panel Discussion**:
- People want cheap food; they don't understand the cost of food production.
- Supermarket consumers by offshore products even if they say they want organic because of the lower price

How are Canadian “consumer needs and wants” served by current government policy and programs ?

Product of Canada

- Standing Policy Committee recommends 85% content for “Product of Canada” labeling
- CFIA & AAFC establish a 98% content requirement and ignore SPC
- Industry can not meet 98% guideline except on a very small number of items. Commodity groups also tell government the objective is unattainable
- Industry removes “Product of Canada” from thousands of items sold in Canada (but not on exports!)
- Canadians can no longer identify safe, healthy Canadian food products from the label.
- Canada goes into a food trade deficit

Additive & Ingredient and new product approvals

- Canada has one of the slowest approval processes in the world. From product approval to labels we lag far behind our competitors with approval times running as much as 2 to 3 years or more

- Omega 3 example from the Maritimes

- AAFC providing funds from Growing Forward to assist Health Canada to speed up the process

CFIA inspection – domestic vs import

- CFIA have insufficient resources to deliver all the protection Canadian consumers require

- Imports are not held to the same standards as Canadian manufacturers – the playing field is not level.

- Product of Canada guidelines have eliminated the consumer’s ability to chose between Canadian and import product

- Canadian processing has stagnated – imports are on the rise – the consumer is voting with their wallet – not survey statements!!

Labeling and Health Claims

- Canada has lagged on approving health claims on food products

- Canadian consumers want to know what the heath benefits of food additives are and are looking to Health Canada to assure them.

- Science is advancing rapidly – Health Canada approvals are not keeping pace – the consumer's desire to "know the benefits" is not being served

Access to capital

- Canadian processors need to modernize and replace labour with capital for productivity improvement
- Traditional lenders will not provide sufficient support to small and medium size processors who must grow to economical scale
- Alberta has pioneered with financial support programs to facilitate modernization and automation and Quebec has followed suit
- AAFC announced a $50 million program to support industry modernization
- If the industry does not become more efficient/competitive the Canadian consumerwill be faced with an even higher ratio of imports in their diets and Canadian farmers will be faced with a further erosion of their domestic customer base

Labour policy

- The industry relies heavily on production labour due in part to access to capital issues.
- There continues to be a labour shortage in this industry in Western Canada – less so in Ontario and Quebec
- Despite higher wages and the higher unemployment rate of the recession Canadians still exhibit no desire to work in this industry
- Foreign workers have been the salvation but Canada has reversed its proactive approach to recruiting and retaining these workers in Canada.
- Labour shortages can and will force some processors to close or relocate

Input costs

- To compete with rising imports Canadian manufacturers must buy competitively priced inputs
- Supply Management can result in higher input costs forcing manufacturers to look elsewhere
- Government policy such as the Bio-fuel subsidies can dramatically increase input costs

Support of “Buy Local”

- Consumer trends support buying locally
- Growing Forward specifically excludes support of local market initiatives
- The AAFC “Brand Canada” initiative will spend over $60 million in overseas markets but only $300 k per year in Canada
- Government policy continues to support commodity export over value added be it domestic or export

Summary

- A strong processing industry is critical to the maintenance of Canada's "Food Sovereignty"
- Food processing recognizes and can provide consumer wants but requires support to remain able to provide for those desires:
- Streamlined regulatory approvals
- Capital support programs for modernization
- Labour policies that recognize the special needs of the industry
- A level playing field

Final Point

Canada lacks a “Food Policy” which links divergent departments towards a common specified objective. We currently have a range of ad hoc policies (often competing with each other) that work against our development to become of one of the strongest Agriculture and Food economies in the world – we are currently slipping further behind. The potential is there if we could develop the vision and the political will to carry it out.