



FCPC INDUSTRY SUSTAINABILITY & COMPETITIVENESS STUDY



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Food and Consumer Products of Canada
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I. EXECUTIVE SUMMARY

This report assesses the financial and economic health of the Canadian food, beverage, and consumer products (“FCP”) industry, using data from a unique, customized survey of the Food and Consumer Products of Canada (FCPC) member companies, Statistics Canada, and additional third-party public sources.¹

FCPC member company respondents provided information about their financial performance, investments in innovation and infrastructure, growth, employment, and perception of industry challenges. The survey data provide a detailed and nuanced understanding of the forces shaping these trends and underscore current challenges to the sustainability of the Canadian FCP industry.

The results of the FCPC Industry Sustainability Study reveal several important challenges for the food, beverage, and consumer products industry, a major sector in Canada. Given the acceleration of certain trends, these challenges reveal important concerns regarding the long-term sustainability of the industry.

The Food, Beverage, and Consumer Products Industry is the Largest Manufacturing Employer and Critical Contributor to the Canadian Economy

- The FCP industry contributed \$28.9 billion to Canada’s GDP in 2017.
- FCP companies are the largest manufacturing employer in Canada with more than 300,000 jobs, accounting together for 16.7% of total manufacturing jobs in Canada (more than the automobile and aerospace industries combined).
- FCP companies in Canada purchase 40% of Canada’s agricultural production.

The Food, Beverage, and Consumer Products Industry Has Been Underperforming in Recent Years Due to a Number of Key Challenges

Despite steady contributions to the Canadian economy, the food, beverage, and consumer products manufacturing sector is punching far below its potential economic weight and lags behind the overall rate of Canadian economic growth.

- Between 2013 and 2017, gross sales² of survey respondents grew at an average annual rate of 1.45% while Canada’s real GDP grew at an average annual rate of 2.12%.³

¹ The Food and Consumer Products of Canada (FCPC) is the largest trade association for the Canadian food, beverage and consumer products industry. See <https://www.fcpc.ca/about-fcpc>, accessed August 17, 2018.

² For ease of exposition, unless otherwise stated, the term “sales” refers to branded sales to retailers exclusively (which account for the majority of total sales among survey respondents) throughout the report.

³ Throughout the report, references are made to values in “real” terms where appropriate. A real value, as opposed to a nominal value, has been adjusted to inflation according to an appropriate price index. Real values allow for more accurate comparisons of the changing value of a bundle of goods, irrespective of inflation-driven price changes.

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- Macroeconomic data show that the cost of farm products and the cost to transport products, which are both critical cost drivers for the food manufacturing sector, have been rising faster than the prices food manufacturers are able to charge for their own products.
 - Despite a favourable exchange rate for manufacturers (lowering the relative costs of production in Canada), Canada has shifted from being a net exporter to a net importer from the United States. This trend has persisted despite the weakening Canadian currency compared to the U.S.

Recent growth appears attributable to company-specific growth — mainly through mergers and acquisitions — rather than industry growth (i.e., a shift in the composition and organization of industry players rather than “organic” growth)

- Between 2015 and 2017, food manufacturers experienced a decline in real sales (dollar-value of sales when accounting for inflation) whereas manufacturers of non-food products experienced modest growth.

Canada is not a favourable environment for innovation in food, beverage, and consumer products manufacturing. Company respondents reported high barriers to market entry such as the high everyday cost of doing business with retailers, high listing fees, high relative costs to manufacture new products, and a burdensome regulatory environment, which reduces the ability and incentives for companies to launch new products and increases the uncertainty surrounding investing in Canada.

- The high everyday cost of doing business with retailers and the cost of promoting products through retailers (taken together, “trade spend”) is increasingly costly for food, beverage, and consumer products manufacturers.
 - Over the past five years, trade spend grew at more than twice the rate of sales.
 - All surveyed FCP companies expect trade spend to continue increasing in the next one to three years, mainly due to the high level of consolidation among retailers.
- The regulatory and administrative costs of doing business in Canada are high. Although Canada performs well in terms of labour market efficiency and the soundness of its banking system, Canadian businesses face the high burden of complex government regulation. These high compliance costs, stemming from increasing and complex regulations may limit innovation.
 - As a report from the Canadian Chamber of Commerce explains: “in an increasingly integrated and highly competitive global economy, multinational corporations have more options than ever about where to invest capital, set up head offices and locate their workforces. If Canada cannot provide a more reliable regulatory environment, new investments and job creation that would have taken place in Canada will happen elsewhere.”
 - A lack of regulatory harmonization between Canada and the U.S. also dampens Canada’s regulatory competitiveness for multinationals operating in both markets.
- Even when innovations are brought to market in Canada, they are not made in Canada: in 2017, 83% of new SKUs launched in Canada were *neither* developed *nor* manufactured

in Canada. In contrast, Canadian manufacturing plants currently produce nearly half of all products sold domestically.

Growth in costs — which outpaces the growth in sales — squeezes margins, limits the profitability of the industry, and dampens the likelihood of future investment in Canada.

- On average, net profit margins for food manufacturers (4.4%) were among the lowest across Canadian manufacturing sectors in 2017. In particular, they were lower than the margins of manufacturers of motor vehicle parts, paper, aerospace products, textiles and apparel.

The number of full-time employees among survey respondents has been decreasing.

- Between 2013 and 2017, full-time employment among company respondents decreased by 7.3%. Assuming this trend was the same for the entire FCP industry, this would equate to a loss of up to 22,000 jobs.
- Qualitative explanations reported by respondents for the decrease in the number of full-time employees include labour relocation or outsourcing certain operations outside of Canada.

Manufacturing capabilities among survey participants appear constant both within and outside of Canada, with little to no change in the total number of company-owned plants used to manufacture products sold in Canada.

These Challenges Threaten the Future Sustainability of the Food, Beverage, and Consumer Products Industry

The FCP manufacturing sector — a critical contributor to Canadian jobs, and to the Canadian economy — is under stress. Accelerating growth in costs has squeezed margins to the point that manufacturers may eventually choose to abandon investing in Canada in favour of other more attractive markets.

Critically, multinational manufacturers produce the majority of products sold on store shelves. These manufacturers examine the relative attractiveness of many markets as they choose to invest (e.g., locate new plants, invest in current plants, and create R&D centres). The uncertainty and the recent relatively poor performance of the Canadian industry puts Canada at a disadvantage when multinational companies consider where to make investments. According to a recent internal FCPC survey:

- Over 65% of multinational respondents reported that their Canadian profit margins were considerably lower than their U.S. or international profit margins.
- The Canadian segment has experienced diminished ROI over the past years. The Canadian market profit margins are dilutive to overall company margins. Respondent companies that serve more than just Canada have an unfavourable view of future investment in Canada due to trade consolidation, cost to serve, and weakening currency. Recent decisions by companies such as Heinz and Campbell's to shut down manufacturing plants in Canada show the impact that these uncertain conditions may have.

Given existing pressures on margins, the business case for investing in Canadian FCP manufacturing is not readily apparent. Although the food, beverage, and consumer products manufacturing sector is critically important to the Canadian economy, our data and analysis clearly show an industry at risk. Without changes to the business environment, the food, beverage, and consumer products industry may diminish substantially — putting Canadian jobs and the economy at risk.

II. INTRODUCTION

This report examines the current financial and economic health of the Canadian food, beverage, and consumer products (“FCP”) industry. To fulfill the mandate of identifying and evaluating the economic factors affecting the supply, production decisions, and competitiveness of the Food and Consumer Products of Canada (FCPC) industry, Analysis Group worked with FCPC stakeholders to develop an empirical approach to quantify and analyze industry health and sustainability.⁴ An in-depth survey of FCPC members, conducted in the second quarter of 2018, based on five years of historical financial performance, is the centrepiece of this analysis.⁵

The report is based on data from FCPC member companies, Statistics Canada, and additional third-party public sources. FCPC member company respondents provided information about their financial performance, investments in innovation and infrastructure, growth, employment, and perception of industry challenges.

An analysis of the FCPC Industry Sustainability Survey results, coupled with an analysis of the relevant macroeconomic data, reveals several important challenges for the FCP industry in Canada. Our results, discussed below, confirm aggregate industry trends visible from macroeconomic data. The study data provide a comprehensive understanding of the forces shaping these trends, as well as underscore current important challenges to the sustainability of the Canadian FCP industry.

III. OVERVIEW OF SURVEYED FCPC MEMBERS

Twenty-six FCPC member companies participated in the FCPC Industry Sustainability Study. Together, these companies account for approximately 40% of total grocery sales in Canada as a whole. The table below summarizes the characteristics of the company respondents. The company participants sample is balanced and representative of FCPC member firms of different sizes and sectors of sales. The vast majority of surveyed firms have been in operation for more than 20 years. Only a small proportion of company respondents are Canadian-owned (12%); most are Canadian subsidiaries of U.S. or multinational companies. In addition to the Canadian market, approximately half of respondents (52%) also serve the United States.

All company respondents sell their products to retailers and approximately half sell to foodservice providers as well.⁶ The most important sales sector in Canada is food, beverage and pet food

⁴ The Food & Consumer Products of Canada (FCPC) is the largest trade association for the Canadian food, beverage and consumer products industry. See <https://www.fcpc.ca/about-fcpc>, accessed August 17, 2018.

⁵ The FCPC Industry Sustainability Survey was launched at the end of March 2018 and remained in the field until June 2018. See survey questionnaire in **Appendix A**.

⁶ Sales to retailers are sales attributable to supermarket, convenience stores, bulk discount stores, and other retailers. These include sales of brand name products (branded sales) and private label products such as in-store brands owned by the retailer (private label sales). This report focuses on an analysis of branded sales to since private label sales and sales to foodservice providers represent a negligible share of the total gross sales among survey respondents.

(73%), followed by health and beauty aids and over-the-counter (19%) and household cleaning/paper goods/general merchandise (8%).

Characteristics of Surveyed FCPC Members, 2018

		% of Participants ^[1]
Most Important Sales Sector in Canada	Food, Beverage and Pet Food	73%
	HaBA / OTC ^[2]	19%
	Household Cleaning / Paper Goods / GM ^[3]	8%
Country of Ownership	Canadian Owned and Operated	11%
	Canadian Subsidiary of U.S. Company	54%
	Canadian Subsidiary of Other Multinational Company	35%
Markets Served ^[4]	Canada	100%
	United States	50%
	Other	15%
Types of Customers ^[5]	Retail	100%
	Foodservice	54%
	Distributors/End Consumers	92%
Time of Operation	≤ 20 years	8%
	> 20 years	92%
Significant Recent Merger/Acquisition	Yes	31%
	No	69%
Full-time Employees in Canada	≤ 500 employees	65%
	> 500 employees	35%
Total Gross Sales to Retailers in Canada	≤ 300 million of Canadian dollars	35%
	> 300 and ≤ 700 million of Canadian dollars	35%
	> 700 million of Canadian dollars	30%
Branded Net Sales to Retailers^[6]	≤ 300 million of Canadian dollars	55%
	> 300 and ≤ 700 million of Canadian dollars	25%
	> 700 million of Canadian dollars	20%

Notes:

[1] Sample includes 26 FCPC members who answered the survey.

[2] HaBA / OTC represents health and beauty aids and over-the-counter products.

[3] GM represents general merchandise.

[4] Several of the survey respondents serve more than one market; the percentages reported are not additive.

[5] Several of the survey respondents serve more than one customer type; the percentages reported are not additive.

[6] Private label net sales to retailers are omitted from the analysis since they account for less than 5% of total sales to retailers among survey respondents.

Source: FCPC Industry Sustainability Survey, 2018.

IV. STUDY RESULTS

This report relies primarily on the results of the FCPC Industry Sustainability Survey. To complement these survey results and provide a complete picture of the FCP industry in Canada, this study also relies on data on Canadian manufacturing sectors and macroeconomic indicators from Statistics Canada and other third-party public sources. An analysis of these combined data reveal the importance of the FCP industry for the Canadian economy and several critical challenges for this key sector in Canada. This section of the report presents a detailed overview of these challenges.

A. The Food, Beverage, and Consumer Products Manufacturing Sector is a Critical Contributor to the Canadian Economy

The food, beverage, and consumer products manufacturing sector is a critical, top contributor to Canadian jobs and to the Canadian economy. It is the largest manufacturing employer in Canada with approximately 300,000 jobs in over 6,000 manufacturing sites across rural and urban areas in Canada.⁷ The sector accounts for 16.7% of total manufacturing jobs in Canada, more than the automobile and aerospace industries combined.⁸

In 2017, the FCP industry contributed \$28.9 billion to Canada's GDP. It is also an important contributor to Canadian exports: the value of the industry's exports grew from \$27.4 billion in 2014 to \$35.8 billion in 2018. Canadian manufactured FCP products are shipped to over 190 countries worldwide.⁹

The agriculture and food sector is among the largest worldwide; Canada is the 11th largest exporter of agriculture and food products.¹⁰ The Canadian government also recognizes this sector as an important player. The 2017 federal budget identified agri-food as a key strategic industry

⁷ See FCPC, "Our Industry" Infographic, available online at: <https://www.fcpc.ca/Portals/0/Userfiles/PAResources/Public%202019/FCPC%20Infographic%20Updated%206500%20EN.pdf?ver=2019-03-26-145353-143×tamp=1553626451637>

FCPC, FCPC, "Value Added - The Future of Food and Consumer Products," available online at: <https://www.fcpc.ca/Portals/0/Userfiles/PAResources/Public%202019/MP%20Package%20for%20WEB%20March%202019.pdf?ver=2019-04-23-111557-893×tamp=1556032565433>

⁸ See FCPC, "Our Industry" Infographic, available online at: <https://www.fcpc.ca/Portals/0/Userfiles/PAResources/Public%202019/FCPC%20Infographic%20Updated%206500%20EN.pdf?ver=2019-03-26-145353-143×tamp=1553626451637>

⁹ See Processed Food and Beverage, NAICS 311, 3121 (locked): <https://www.ic.gc.ca/eic/site/tdo-dcd.nsf/eng/home>

¹⁰ See Advisor Council on Economic Growth, "Unleashing the Growth Potential of Key Sectors", February 6, 2017, available online at: <https://www.budget.gc.ca/aceg-ccce/pdf/key-sectors-secteurs-cles-eng.pdf>

with “great potential for growth and job creation.”¹¹ The FCP industry purchases 40% of Canada’s agricultural production.¹² Further, over 60% of the industry’s output is sold to Canadians through grocery stores and restaurants.¹³

Given the significance of this industry for the Canadian economy and its implications for consumers as well as other related sectors (e.g., the agricultural sector, grocery retailers), it is therefore important to identify and evaluate the economic factors affecting the supply, production decisions, and long-term sustainability of this manufacturing industry.

B. The Food, Beverage, and Consumer Products Industry Has Recently Been Underperforming Due to a Number of Challenges

Despite being such an important sector for the Canadian economy, an analysis of the FCPC Industry Sustainability Survey results—in combination with publicly available data—reveals many important challenges for the FCP industry in Canada. In recent years, the industry has been underperforming in a number of areas: modest growth in revenue and profits, limited Canadian innovation, increasing costs and trade spend, and shifts in the employment landscape.

1. Challenge #1: The food, beverage, and consumer products manufacturing sector is punching far below its potential economic weight

An examination of Canadian macroeconomic data shows that the FCP industry has been underperforming relative to the overall Canadian economy in the past few years. This recent poor performance is likely related to a number of macroeconomic factors such as fluctuations in the Canada-U.S. exchange rate and increases in input costs and transportation costs.¹⁴

Over the past decade, the Canadian economy has performed relatively well. Gross domestic product (GDP) growth has been positive, strong, and similar to that of the United States. Since the Great Recession in 2008 and 2009, Canada’s economy has recovered and expanded at a relatively modest but steady rate of 1% to 3% per year (**Figure 1.1**).

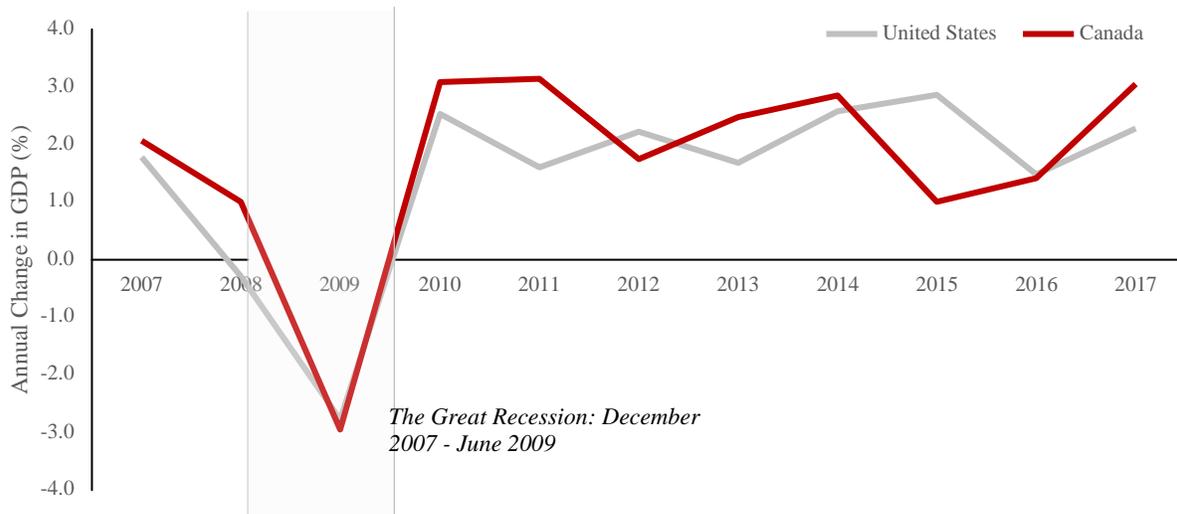
¹¹ See FCPC, Impact Report 2017, available online at: <https://www.fcpc.ca/News/View/ArticleId/364>.

¹² See FCPC, Impact Report 2017, available online at: <https://www.fcpc.ca/News/View/ArticleId/364>.

¹³ See Agriculture and Agri-Food Canada, “Food Processing Industry Roundtable”, 2017, available online at <http://www.agr.gc.ca/eng/industry-markets-and-trade/value-chain-roundtables/food-processing/?id=1385742632592>

¹⁴ Other factors are discussed later within this section.

Figure 1.1
Year-over-year Real GDP Growth, Canada and the United States, 2007 – 2017



Notes:

[1] The above figure presents the annual change in real GDP for Canada and the United States between 2007 and 2017.

[2] Underlying real GDP values used for calculation are in constant 2010 USD for comparability.

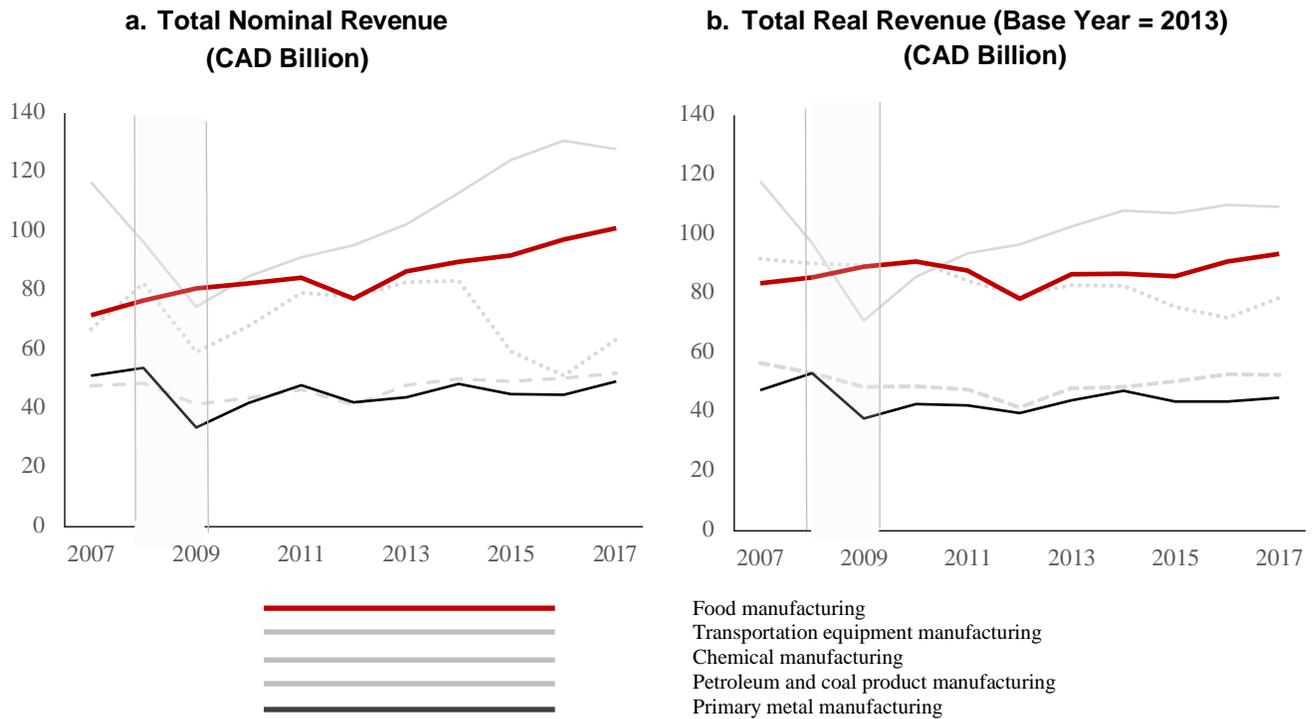
Source: The World Bank – World Development Indicators (World Bank national accounts data); <http://databank.worldbank.org/data/source/world-development-indicators#>; accessed Jul 17, 2018.

Although a key contributor to the Canadian economy, the food manufacturing sector has recently been performing modestly according to macroeconomic data. Between 2007 and 2017, the food manufacturing industry saw, on average, an annual increase in revenue of 1.12% (**Figure 1.2**). This performance was similar to that of other major manufacturing sectors, namely transportation equipment, petroleum and coal products, chemicals, and primary metals. All of these sectors have experienced flat or modest growth in total real revenue over the past few years (**Figure 1.2**).

More importantly, the food, beverage, and consumer products manufacturing sector lags the overall rate of economic growth. Between 2013 and 2017, gross sales of survey respondents grew at an average annual rate of 1.45% while Canada’s real GDP grew at an average annual rate of 2.08%, suggesting that this industry underperformed compared to the overall Canadian economy.¹⁵

¹⁵ See next section for additional details on survey respondents’ reported growth in gross sales.

Figure 1.2
Total Revenue in Canadian Manufacturing Sectors, 2007 – 2017



Notes:

- [1] The above figure depicts total (a) nominal and (b) real industry revenues for food manufacturing compared to other major manufacturing industries.
- [2] For manufacturing sectors, nominal values are deflated according to the relevant Industry Product Price Index (IPPI).
- [3] The highlighted section of the graph covers the Great Recession, from approximately December 2007 to June 2009.

Sources:

- [1] Statistics Canada. Manufacturers' sales, inventories, orders and inventory to sales ratios, by industry; Table 16-10-0047-01.
- [2] Statistics Canada, Industrial product price index, by industry; 18-10-0032-01.

Although growth in local demand for food is somewhat restricted by Canada’s population growth, the Canadian FCP sector (as part of the larger agri-food sector) has significant global growth potential. Given Canada’s natural resources required for food production (e.g., arable land, water) and favourable global food demand, this sector has the potential to contribute more significantly to Canada’s GDP growth by virtue of becoming a global supplier of value-added agricultural products.¹⁶ However, despite the rising economic tide, factors such as unpredictable and fluctuating Canada-U.S. exchange rates, increasing input costs, and increasing transportation

¹⁶ See Advisor Council on Economic Growth, “Unleashing the Growth Potential of Key Sectors”, February 6, 2017, available online at: <https://www.budget.gc.ca/aceg-ccce/pdf/key-sectors-secteurs-cles-eng.pdf>

costs exert economic pressure on the Canadian food, beverage, and consumer product manufacturing industry.

1.1 Fluctuating Canada-U.S. exchange rate

Canadian consumers have faced an unfavourable exchange rate since early 2013, peaking at 1.38 CAD for 1.00 USD in January 2016 (Figure 1.3). However, the depreciation of the Canadian dollar could provide cost and price advantages for Canadian manufacturers relative to U.S. manufacturers; a weak Canadian dollar could favour manufacturers who export to the United States and manufacturers who sell to Canadian retailers. In contrast, for Canadian manufacturers who import raw materials from the United States, the depreciation of the Canadian dollar implies that the price of their inputs are getting more expensive. As discussed in later sections, the recent increased consolidation in the retail sector limits the ability of Canadian FCP manufacturers to partially offset these price increases by raising the price charged to retailers.

Figure 1.3
Canadian Dollar per U.S. Dollar, 2007 – 2017

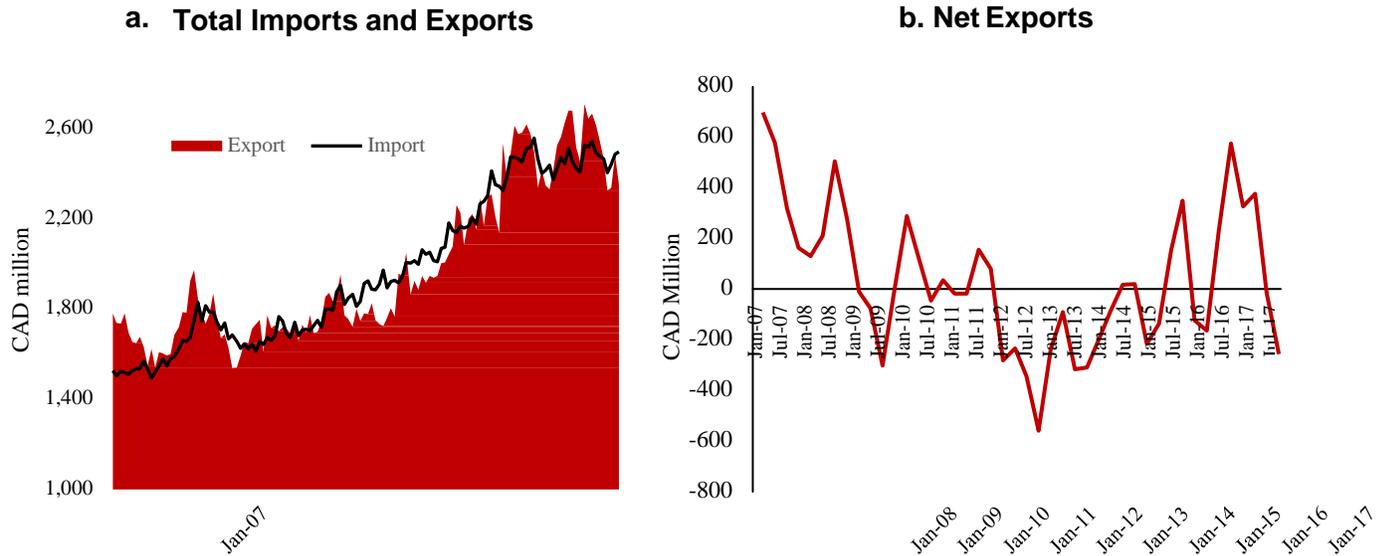


Note: The above figure plots the monthly average exchange rate between Canada and the United States

Source: Federal Reserve Economic Data (FRED), <https://fred.stlouisfed.org/series/EXCAUS>; accessed on August 8, 2018.

Contradictory to traditional economic expectations regarding the balance of trade in the presence of a depreciated Canadian dollar, Canada’s imports of food, beverages, and tobacco products exceeded exports for most of 2012 to 2015 and again in the first half of 2016 and the second half of 2017 (Figure 1.4). Indeed, imports of food, beverages, and tobacco products have been greater than exports suggesting that retailers and producers manufacture more products in the United States (or elsewhere) for Canadian consumption. Hence, despite a favourable exchange rate for manufacturers (lowering the relative costs of production in Canada), Canada has shifted from being a net exporter to a net importer from the United States. This trend has persisted despite the increasing strength of the USD compared to the CAD.

Figure 1.4
Exports and Imports of Food, Beverages, and Tobacco Products, 2007 – 2017



Notes The above figure plots Canada’s (a) imports and exports of food, beverages, and tobacco products for use as consumer goods and (b) net exports equal to exports minus imports. All values are in constant 2013 CAD.

Sources:

- [1] Statistics Canada, International merchandise trade by commodity; Table 12-10-0001-01.
- [2] CPI: Statistics Canada (<https://www150.statcan.gc.ca/n1/pub/62-001-x/2018004/tbl/tbl-5-eng.htm>).

1.2 Increasing costs of inputs

Further, macroeconomic data also show that the cost of farm products (as measured by the Farm Products Price Index) and the cost to transport products — two critical cost drivers for the food manufacturing sector — have been rising faster than prices food manufacturers can charge for their own products.

Between 2007 and 2017, production costs for the food manufacturing industry were rising. **Table 1.5** shows the increase in inputs (what food manufacturers need to pay to make their products) compared to the increase in the price of outputs (what food manufacturers can charge for their products). The Industry Product Price Index (IPPI) for food manufacturing measures the price received by food product manufacturers (i.e., output prices). The input prices for food manufacturers are represented by the Farm Products Price Index (FPPI) and the Raw Materials Price Index (RMPI), as both farm products and raw materials are key inputs for food

manufacturing.^{17, 18} Between 2007 and 2017, both input prices and output prices were rising; however, output prices likely did not increase enough to counterbalance the increase in input prices. The IPPI increased at annual growth rate of 2.24% between 2007 and 2017, while the RMPI and the FPPI increased at an annual rate of 2.41% and 0.9%, respectively. If it is the case that the costs of inputs are increasing faster than output prices, then profit margins in the food manufacturing sector are likely being squeezed, thereby reducing the incentive for companies to invest in the Canadian market.

Table 1.5
Industry Costs Indices Evolution, 2007 – 2017
(Base year = 2013)

Index	Average Annual Growth Rate (%)	Differential with IPPI Average Growth Rate (Percentage point)
IPPI (Output)	2.24 %	
FPPI (Input)	2.71%	+0.47
RMPI (Input)	0.9%	-1.34

Note: Output price fluctuations measured by the Industrial Product Price Index (IPPI). Input prices measured by the Farm Products Price Index (FPPI) and the Raw Materials Price Index (RMPI) excluding movements in the price of crude oil.

Sources:

- [1] Statistics Canada, Industrial product price index, by product; Table 18-10-0030-01.
- [2] Statistics Canada, Farm products price index; Table 32-10-0099-01.
- [3] Statistics Canada, Raw materials price index; Table 18-10-0034-01.

1.3 Increasing costs of transportation

As food products can be bulky, heavy, and/or perishable, the food manufacturing industry is also sensitive to fluctuations in the price of transportation, which affects both the cost of inputs and the

¹⁷ As per Statistics Canada, “[t]he Farm Products Price Index (FPPI) measures the changes in prices that farmers receive for the agriculture commodities they produce and sell. Commodities are priced at point of first transaction, where the fees deducted before a producer is paid are excluded... The universe includes all Canadian agriculture operations as defined by the Census of Agriculture.”

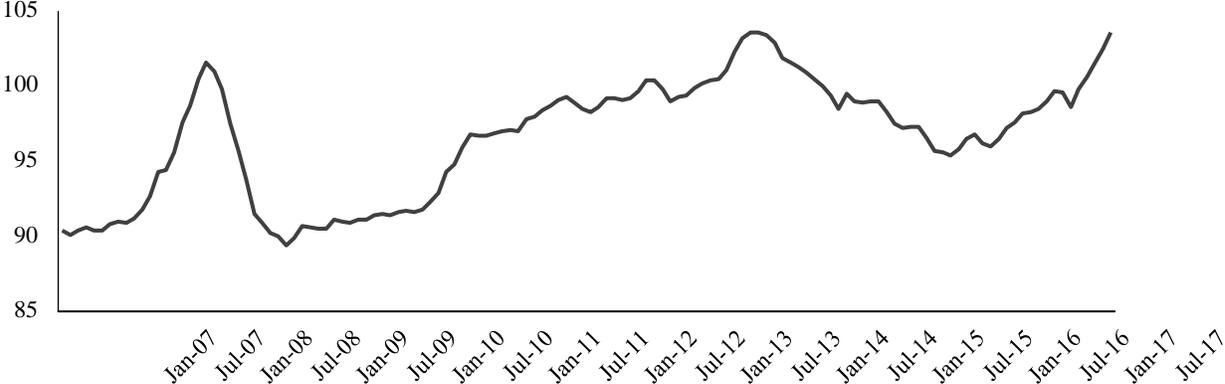
(Source: <http://www23.statcan.gc.ca/imdb/p2SV.pl?Function=getSurvey&SDDS=5040>)

¹⁸ As per Statistics Canada, “[t]he Raw Materials Price Index (RMPI) measures price changes for raw materials purchased by industries in Canada for further processing. As a purchasers’ price index, prices include all charges purchases incur to bring a commodity to the establishment gate. ... The target population of the RMPI consists of those manufacturing establishments residing and producing in Canada.”

(Source: <http://www23.statcan.gc.ca/imdb/p2SV.pl?Function=getSurvey&SDDS=2306>)

cost of final goods. Transportation costs in Canada are on the rise, in real terms. **Figure 1.6** shows, as measured by the For-hire Motor Carrier Freight Services Price Index,¹⁹ that the average price paid to transport products in Canada increased by 15% between 2007 and 2017. The rise of transportation costs is another factor that may have put pressure on FCP manufacturers' profitability margins in recent years.

Figure 1.6
For-hire Motor Carrier Freight Services Price Index, Truck Transportation,
2007 – 2017 (Real 2013 CAD)



Note: The For-hire Motor Carrier Freight Services Price index measures the movement of prices for the services that are provided by the trucking industry.

Source: Statistics Canada, For-hire Motor Carrier Freight Services Price Index, Table 18-10-0043-01.

Overall, persistent and large differences between the United States and Canada affect the degree to which products from the U.S. will be substituted for products from Canada. Fluctuations in the Canada-U.S. exchange rate as well as increasing farm product, raw material, and transportation costs have likely contributed to the recent underperformance of the Canadian food, beverage, and consumer product manufacturing industry relative to the Canadian economy as a whole. Although the FCP industry is still fairly stable economically, these macroeconomic trends suggest persistent, growing risks that pose a threat for the long-term economic health of the industry. The results of our customized survey, discussed next, also point to the sustainability of the industry being at risk.

2. Challenge #2: Canada is a challenging environment for “organic” growth in the food, beverage, and consumer products manufacturing sector

A company’s gross sales correspond to the total of all sale transactions before any adjustments for discounts, deductions, or for the costs incurred in generating those sales. Growth in gross sales are thus a strong indicator of growth in the total amount of products sold by companies (i.e.,

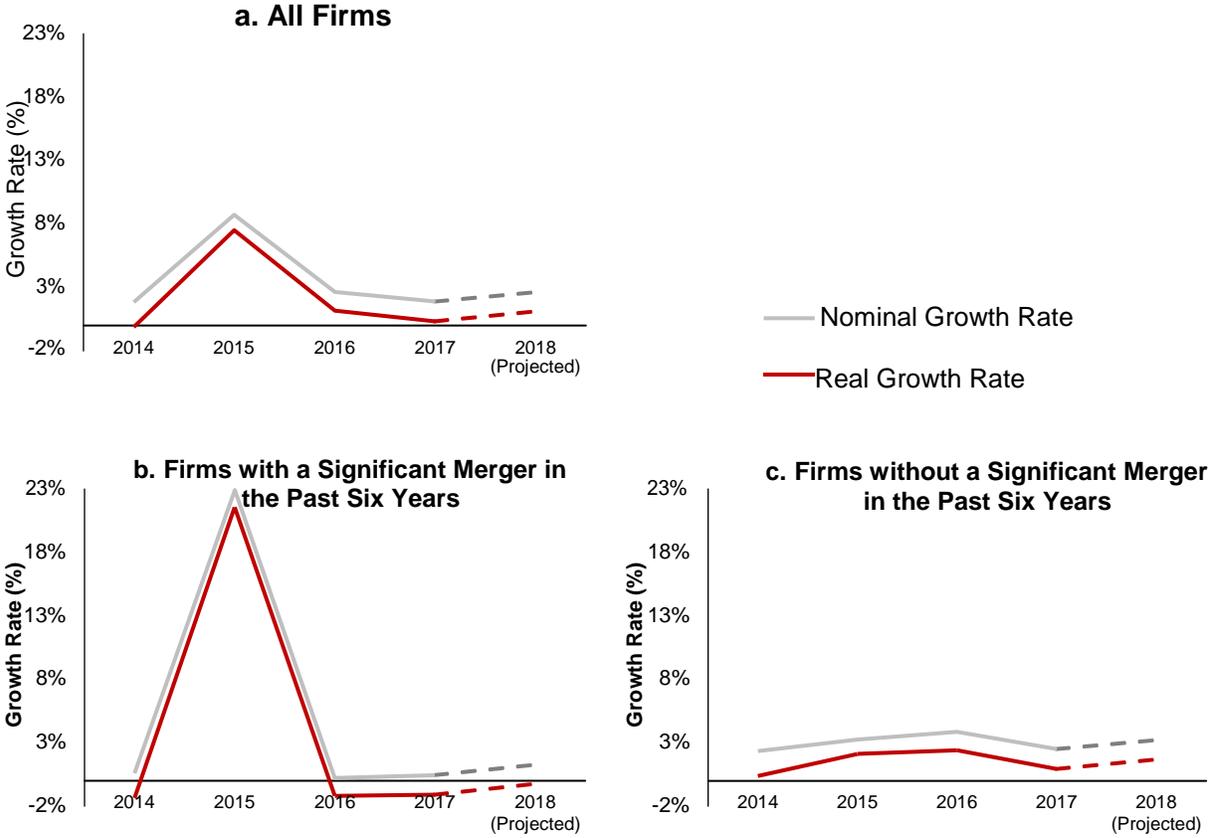
¹⁹ The For-hire Motor Carrier Freight Services Price Index is constructed by Statistics Canada and is based on the prices for the services that are provided by the trucking industry. See Statistics Canada, available online at <http://www23.statcan.gc.ca/imdb/p2SV.pl?Function=getSurvey&SDDS=5136>.

growth in revenue). As such, gross sales are also an indicator of customer demand for the company’s products and have a large impact on profitability.

A quantitative analysis of company respondents’ data on gross sales to retailers reveals that gross sales increased consistently — but modestly — between 2013 and 2017 at an average annual rate of 2.21% per year (**Figure 2.1**). However, growth mainly stems from a spike in gross sales that occurred in 2015, when real gross sales increased by 7.54% in 2015 (**Figure 2.1a**). This large jump in sales appears to be explained by mergers and acquisitions (M&A) activity rather than industry growth (i.e., a shift in the composition and organization of industry players rather than “organic” growth).

When excluding firms that experienced significant growth-by-merger in the past six years, gross sales only grew at an average annual rate of 1.45% over the 2013–2017 period (**Figure 2.1c**). In comparison, over the same period, Canada’s real GDP grew at an average annual rate of 2.12%. Hence, when controlling for merger effects, real gross sales increased at a slower pace than real GDP over this period, suggesting that the FCP industry underperformed compared to the overall Canadian economy.

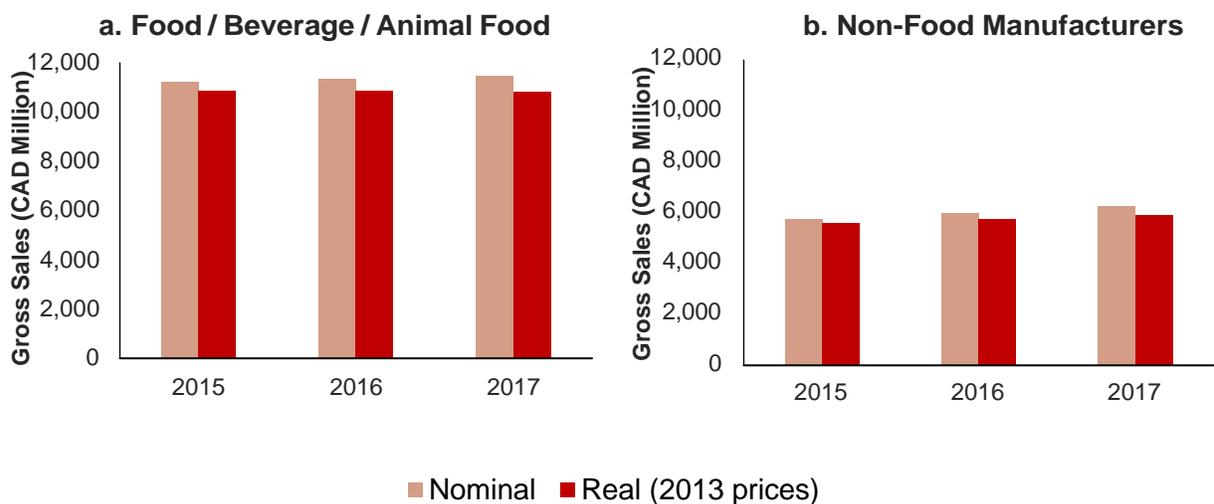
Figure 2.1
Growth in Sales in Canada, 2014-2018



Note: Charts include data from 21 survey respondents with sufficient data across displayed years (12 firms without a merger, 9 with a merger within the past 6 years).
Source: FCPC Industry Sustainability Survey, 2018.

Non-food manufacturers — those survey respondents reporting health and beauty aids and over-the-counter (“HaBA/OTC”) and household cleaning, paper goods, or general merchandise (“Household / Cleaning Goods / GM”) as their most important sales sector — performed better than food manufacturers in the past five years (**Figure 2.2**). During the post-merger period (2015–2017), non-food manufacturers maintained a modest 2.78% average annual growth rate in sales.²⁰ In comparison, after controlling for inflation, food manufacturers saw their sales actually *decrease* by 0.29% over the same period (**Figure 2.2**).²¹ Any recent growth in food manufacturing sales therefore appears inflation-driven, as real industry sales are declining. In our qualitative analysis of factors contributing to poor sales performance, company respondents cited changing customer preferences resulting in declining customer consumption in certain FCP categories and increased competition from e-commerce, private labels, and foodservice brands as factors inhibiting growth.

Figure 2.2
Sales in Canada, by Most Important Sector of Sales, 2015 – 2017



Note: Chart includes data from the 23 companies with sufficient data. (15 food manufacturers, 8 non-food manufacturers)
Source: FCPC Industry Sustainability Survey, 2018.

²⁰ The period 2015–2017 is used to eliminate the effect of mergers in 2013 mergers and to present results based on a larger number of respondents. Some respondents did not provide data prior to 2015, so using the shorter timeframe (2015–2017) increases the sample size.

²¹ As mentioned above, for both food and non-food manufacturers combined (excluding firms that experienced a significant merger in the past six years), the overall average annual growth rate in sales over the 2013-2017 period is 1.45%.

3. Challenge #3: There are many barriers to innovation in Canada

Innovation may be product-related (e.g., developing new consumer products, line extensions, entry into a new product category) or process-related (e.g., developing new production techniques). In particular, product innovations help ensure that Canadian consumers are getting the best products, and indicate a healthy business environment for FCP industry participants. However, FCP manufacturers appear to be facing poor incentives to innovate in Canada due to a variety of factors such as the high everyday cost of doing business with retailers, high listing fees, high relative costs to manufacture new products, and a burdensome regulatory environment.

3.1 Product innovation in Canada

Product innovations are new products brought to the market (e.g., new products resulting from new formulas, new flavours, or new products entering a category).²² Canada does not appear to be a favourable environment for innovation in the FCP manufacturing sector. Two out of three respondents reported that the majority of their company's innovations over the past one to three years took place outside of Canada.²³ Moreover, in the past one to three years, 75% of company respondents have decided not to launch several new products (more than five) in Canada that they launched in other countries.

Even when new innovations are brought-to-market, they are not made in Canada. Among the 2,490 SKUs intended for retail customers that were introduced by company respondents in Canada in 2017, 83% were *neither* developed *nor* manufactured in Canada. Whereas company respondents reported that their Canadian manufacturing plants currently produce nearly half of all domestic sales, only 11% of newly introduced SKUs were both developed and manufactured in Canada (Table 3.1).

Table 3.1
Number of Innovative SKUs Intended for Retail Customers Introduced in Canada in 2017

Location	Count of SKUs	Percentage of SKUs
Developed and manufactured in Canada	264	11%
Developed, but not manufactured in Canada	107	4%
Manufactured, but not developed in Canada	57	2%
Neither developed nor manufactured in Canada	2,062	83%
Total	2,490	100%

Note: Table includes data from the 23 companies with sufficient data.

Source: FCPC Industry Sustainability Survey, 2018.

²² For the purposes of this study, product innovations are defined as new SKUs that were introduced as a result of new products. New SKUs that are the result of repackaging and/or re-sizing of existing products are excluded from the reporting and, therefore, from our analysis.

²³ This percentage remains the same (65%) when only considering U.S. or internationally owned companies.

Qualitatively, many survey respondents reported high barriers to launching new products in the Canadian market, mentioning barriers such as the high everyday cost of doing business with retailers, high listing fees, a high relative cost to manufacture new products, and a burdensome regulatory environment. High listing fees in particular is a widespread concern: 80% of survey respondents reported that listing fees had an impact on their decision to innovate or invest in Canada in the past one to three years. Of this group, 95% reported a negative impact of listing fees on innovation and/or investment in Canada.²⁴ For example, one respondent mentioned that listing fees are a deciding factor when launching a new product in Canada because they constitute “high barriers to [enter] the market, limiting experimental launches.” Another respondent agreed: “Cost of entry (innovation) is high and significantly reduces innovation.” A third respondent explained that they “have had excellent products ready to launch, but cannot due to the burden of [regulatory agencies].”

3.2 A burdensome regulatory environment

Regulatory and administrative costs of doing business in Canada are high. To avoid being a hurdle to innovation, regulations should be consistent, predictable, and efficient; however, businesses in Canada face complex, overlapping regulations at several levels of government.²⁵ There were 131,754 federal requirements for businesses operating in Canada in 2015, up from 129,860 in 2014. In addition, Ontario alone, for example, has more than 380,000 regulations.²⁶

According to the Global Competitiveness Index developed by the World Economic Forum, which measures competitiveness via productivity improvements, Canada’s position dropped from 9th to 14th among the 137 countries considered over the past six years. Although Canada performs well in terms of labour market efficiency and the soundness of its banking system, Canadian businesses face a high burden of complex unpredictable government regulation, creating an uncertain environment.²⁷ According to another index developed by the World Economic Forum, businesses in Canada face a high burden of government regulation, ranking 38th worldwide, lagging behind notably Germany (7th), the United States (12th), and China (18th).²⁸ The same conclusion is supported by an analysis from the World Bank.²⁹

Further, because the U.S. is Canada’s most important trading partner, a lack of regulatory harmonization between the two countries dampens Canada’s regulatory competitiveness for

²⁴ Specifically, 20/25 reported that listing fees had an impact on their decision to innovate or invest in Canada in the past one to three years. Of those 20, 19 respondents reported a negative impact and one respondent reported a neutral impact.

²⁵ See Chamber of Commerce Report, pp. 2 and 39.

²⁶ See The Canadian Chamber of Commerce, “Death by 130,000 Cuts: Improving Canada’s Regulatory Competitiveness”, May 2018, p.1, available online at: http://www.chamber.ca/advocacy/regulate-smarter-toolkit/DRAFT_DeathBy130000Cuts_ImprovingCanadasRegulatoryCompetitiveness.pdf (hereafter “Chamber of Commerce Report”).

²⁷ See Chamber of Commerce Report, pp. 2 and 6.

²⁸ See Chamber of Commerce Report, p.6.

²⁹ See Chamber of Commerce Report, p.7.

multinationals operating in both markets.³⁰ A report by the Canadian Chamber of Commerce explains: “[...] in an increasingly integrated and highly competitive global economy, multinational corporations have more options than ever about where to invest capital, set up head offices and locate their workforces. If Canada cannot provide a more reliable regulatory environment, new investments and job creation that would have taken place in Canada will happen elsewhere.”³¹

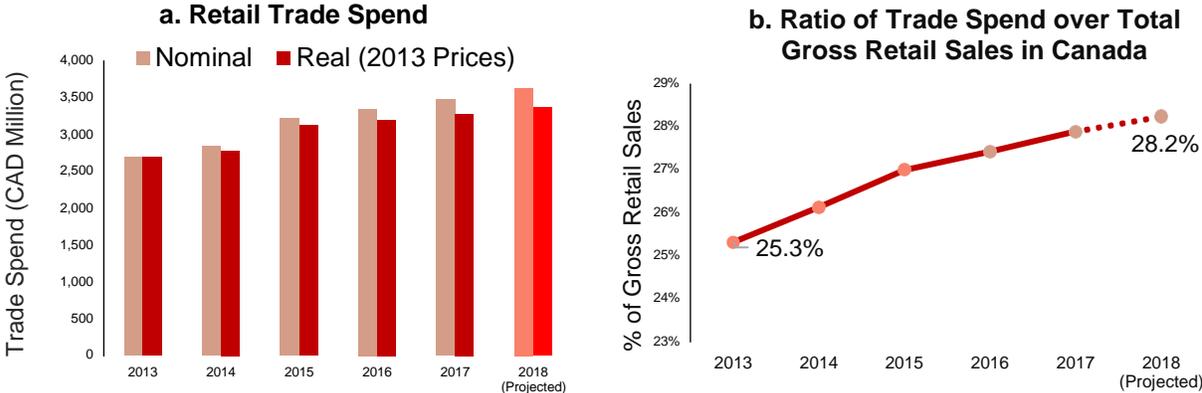
For FCPC members, regulatory challenges include notably recent regulations or discussions concerning front-of-package labelling, restricted marketing/advertising for children, user fee regimes required for certain service deliveries.³² Overall, onerous compliance costs and the increasing number and complexity of new regulations may therefore limit innovation and investments in Canada.

3.3 Increasing trade spend

The everyday cost of doing business with customers and cost of promoting products through retailers — trade spend — is increasingly costly for food, beverage, and consumer products manufacturers; this may be a barrier to innovation. Anecdotal information indicates that FCP manufacturers generally spend more on trade spend in Canada than in other countries. PricewaterhouseCoopers has estimated that retail trade spend, as a percentage of gross sales, is 18% in the United States.³³ In 2017, this percentage was 28% in Canada.

For Canadian FCP manufacturers, trade spend grew at more than twice the rate of sales over the past five years. Specifically, between 2013 and 2017, real trade spend grew 22% (for an average annual growth rate of 5.1%) among respondents who provided data across all years (**Figure 3.2**).

Figure 3.2 – Retail Trade Spend in Canada, 2013-2018



Note: The left chart was created from the 19 survey respondents who provided data across all years for both variables
Source: FCPC Industry Sustainability Survey, 2018.

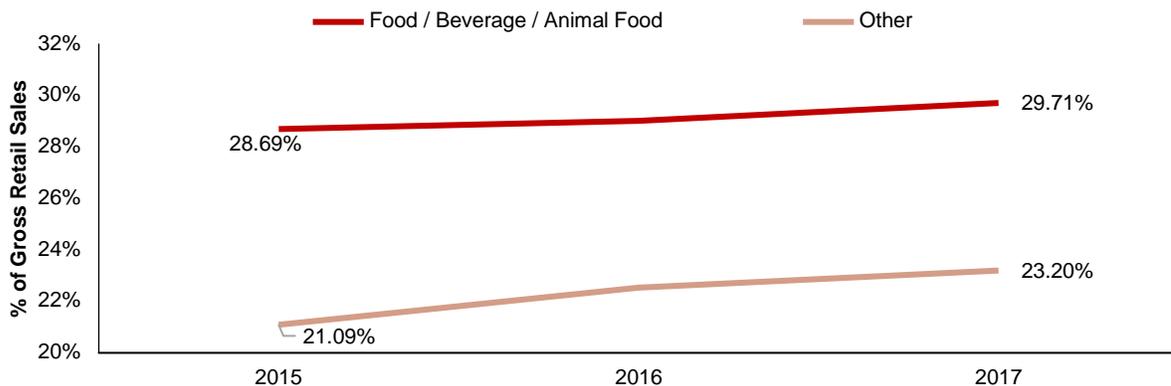
30 See Chamber of Commerce Report, p.8.

31 See Chamber of Commerce Report, p.9.

32 See FCPC, “Value Added - The Future of Food and Consumer Products,” available online at: <https://www.fcpc.ca/Portals/0/Userfiles/PAResources/Public%202019/MP%20Package%20for%20Web%20March%202019.pdf?ver=2019-04-23-111557-893×tamp=1556032565433>

33 See PwC/Strategy & 2016 Customer Planning and Trade Spend Management Study.

Figure 3.3
Retail Trade Spend as a % of Gross Sales, by Sector of Sales, 2015 – 2017



Notes:

[1] The chart was created from the 22 survey respondents who provided data for 2015, 2016, and 2017.

[2] Of those, 15 declared *Food / Beverage / Animal Food* as their main sector of sales, 7 did not.

Source: FCPC Sustainability Survey, 2018.

When examining trade spend by respondents’ main sector of sales, food manufacturers appear to face higher trade spend costs than non-food manufacturers. **Figure 3.3** shows that there is a large gap in trade spend (as a percentage of gross sales) between the two types of manufacturers. Between 2015 and 2017, the share of food producers’ retail trade spend rose from 28.7% of gross sales to 29.7%. In comparison, the share of non-food producers’ retail trade spend rose from 21.1 % of gross sales to 23.2% (**Figure 3.3**). While the increase is larger for non-food manufacturers, the burden of trade spend remains greater for food manufacturers.

Qualitative answers from surveyed FCP industry participants highlight that increasing trade spend costs are an important concern for both food and non-food manufacturers. Surveyed FCP industry participants do not expect any relief in the future; as all 26 survey respondents expect trade spend to increase in the next one to three years. Increased consolidation among retailers (which has decreased manufacturers’ ability to negotiate with retailers) is a widespread concern for survey respondents. When asked why they expect trade spend to increase in Canada, retailer consolidation was cited most often (by over a third of respondents). In particular, one respondent explained: “Trade spend will increase given the past historical trend to do so based on the consolidation of the retail and food service industry and their significant leverage on the manufacturer[s] to extract additional fees and limit pricing to recover those fees.” Another responded added: “With increased consolidation and channel shift to e-commerce, traditional retail customers are becoming increasingly demanding to the point where you either accept their demands for higher trade spend or lose support and face delists.”

Hence, the Canadian FCP industry does not appear to be getting a return on its increasing investments in retailer trade spend. Net retail sales are defined as gross retail sales less cost-to-serve, which corresponds to the sum of trade spend, customer marketing, and trade fines and fees. The slow to shrinking growth in real gross sales (particularly for food manufacturers) highlighted in the previous section, combined with increasing trade spend, has resulted in flat net

sales between 2015 and 2017. In fact, since trade spend is increasing at a faster rate than gross sales, flat net sales could suggest a decrease in other cost-to-serve spending such as marketing spending. As discussed in the next section, flat net sales combined with increasing production costs considerably limit FCP manufacturers' profitability resulting in reduced capital investment in the Canadian economy.

4. Challenge #4: The increasing cost of goods sold (COGS) limits manufacturers' growth in profitability

Prospects for profitability growth depend on current revenue levels as well as potential future revenue (for instance through innovation), but they also rely on current and expected expenses accrued throughout the process of generating products. An analysis of the cost of goods sold (COGS)³⁴ among FCP industry participants reveals that this cost has been increasing at a faster rate than the total of gross sales. For these manufacturers, the increasing COGS, combined with growing difficulties in passing along these cost increases to retailers, has limited their growth in profitability in recent years and may reduce future investments in the Canadian market.

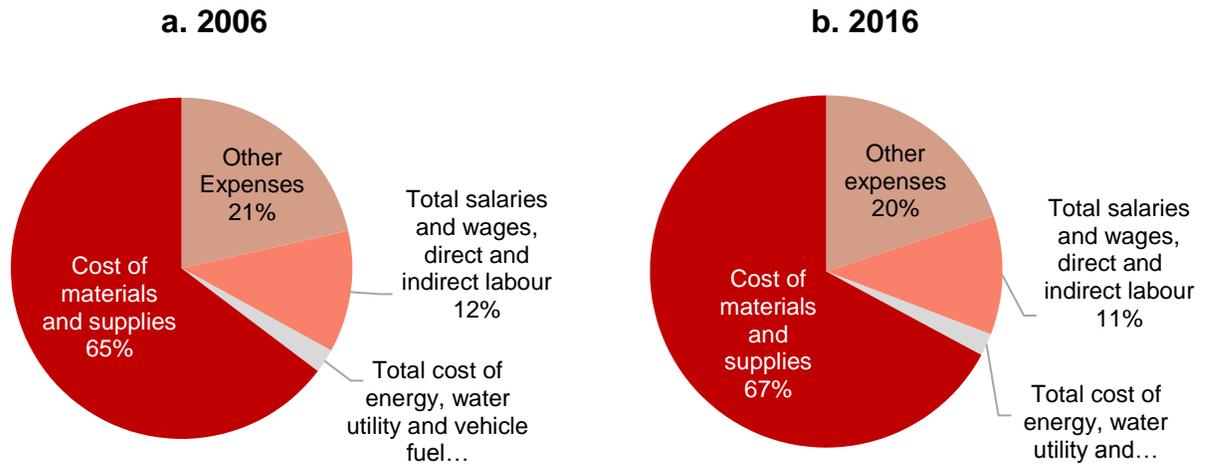
Statistics Canada data show that the relative contribution of different categories of costs has largely remained stable over the last decade. The breakdown of food manufacturing costs into (i) costs of materials and supplies, (ii) costs of energy, water utility, and vehicle fuel, (iii) salaries and wages, and (iv) other expenses did not change between 2006 and 2016 (**Figure 4.1**).³⁵ The largest cost component for food manufacturers has consistently been the cost of materials and supplies. As such, any fluctuations in the price of raw materials (as measured by the FPPI and the RMPI) can have large impacts on a food manufacturing firm's costs.³⁶

³⁴ The cost of goods sold (COGS) is defined as the sum of the cost of materials (e.g. raw materials, packaging), conversion costs (e.g., direct labour [i.e., manufacturing-related], factory related depreciation, and other manufacturing costs), and costs of imported finished foods. These do not include trade spend.

³⁵ As of November 1, 2018, data on the breakdown of food manufacturing costs for 2017 was not available.

³⁶ See Section IV.B.1 for additional details on the Farm Products Price Index (FPPI) and the Raw Materials Price Index (RMPI).

Figure 4.1
Breakdown of Food Manufacturing Costs, 2006 – 2016

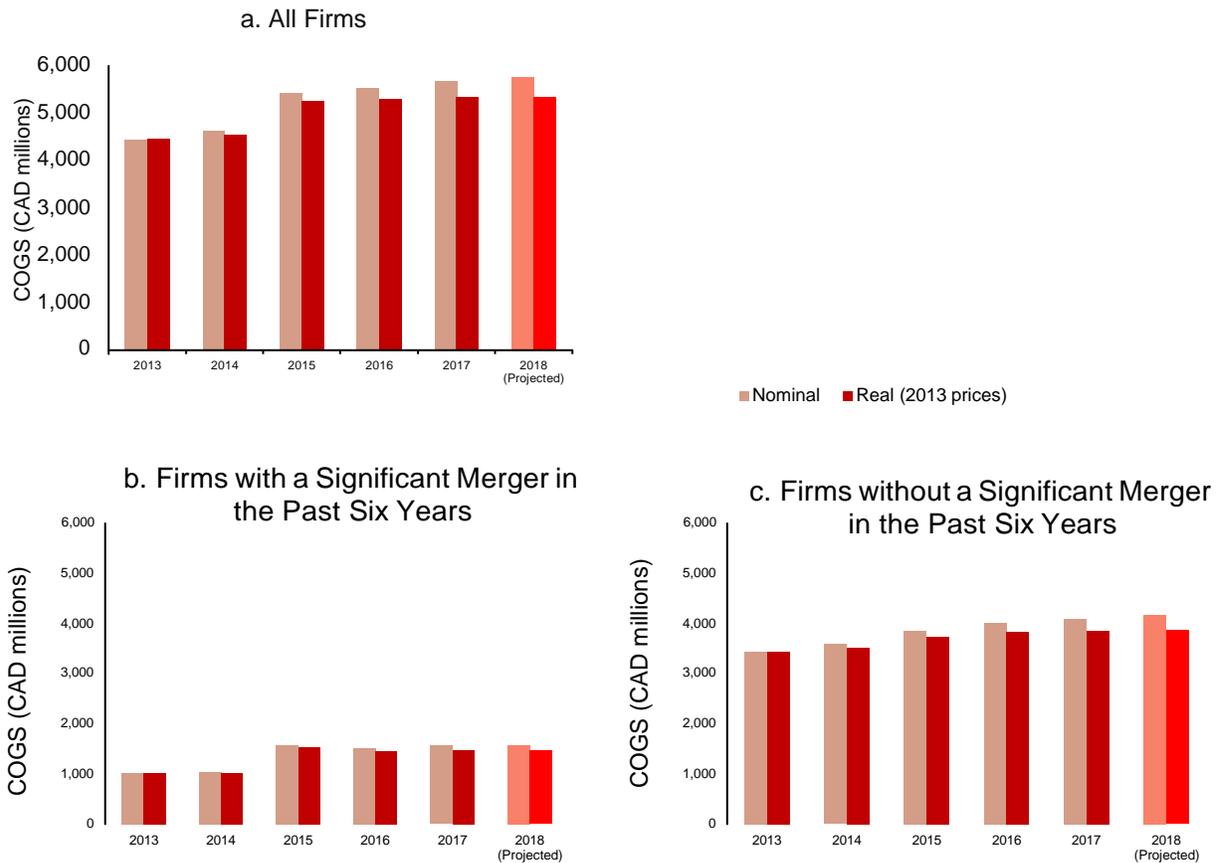


Sources:

- [1] Statistics Canada, Principal statistics for manufacturing industries; Table 16100117. (Data for 2012 –2016).
- [2] Statistics Canada, Principal statistics for manufacturing industries; Table 16-10-0038. (Data for 2006 –2011).

Among survey respondents, the cost of goods sold (COGS) increased by 2.26% between 2013 and 2017 (**Figure 4.2**). Moreover, the COGS grew at a faster rate than that of gross sales, thereby negatively affecting margins (**Figures 4.2 and 4.3**).

Figure 4.2
COGS, 2013-2018



Notes:

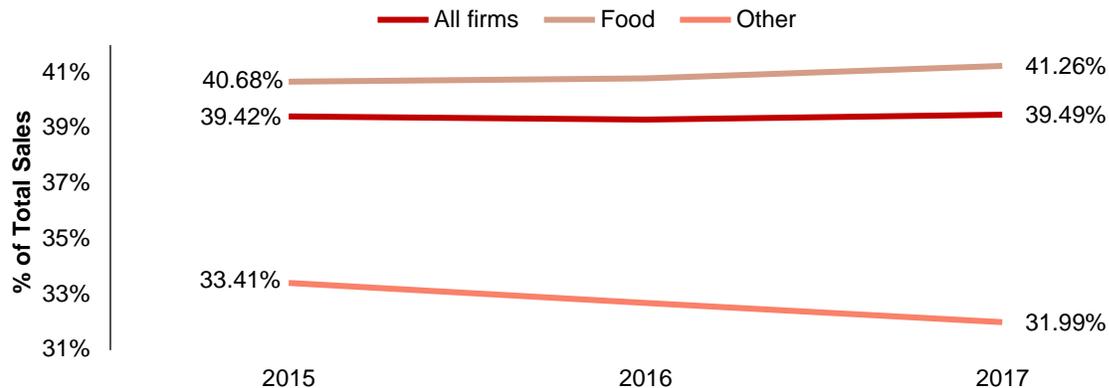
[1] The charts were created from the 18 survey respondents who provided data across all years.

[2] Of those, 12 firms had no merger and 6 firms experienced a merger within the past 6 years.

Source: FCPC Industry Sustainability Survey, 2018.

Food manufacturers' COGS represents a larger proportion of their gross sales than the COGS of non-food manufacturers. Indeed, the COGS only corresponds to 32% of gross sales for non-food producers, while it corresponds to 41% for food producers (**Figure 4.3**). The fact that the price index of farm products in Canada (FPPI) is higher than the index for raw materials (RMPI) could explain this gap. Food manufacturers have experienced an increase of 0.6 percentage point in this ratio between 2015 and 2017. In the same period, the ratio for non-food manufacturer declined by 1.4 percentage point. If these trends remain the same, this gap may continue to widen.

Figure 4.3
COGS as a Percentage of Total Gross Sales in Canada, by Main Sector of Sales, 2015 – 2017



Note: Chart includes data from 20 companies with sufficient data across all years (15 food manufacturers, 5 non-food manufacturers)

Source: FCPC Industry Sustainability Survey, 2018.

FCP manufacturers are concerned about these cost increases. The study collected qualitative information on major challenges faced by participants in the past one to three years. When asked about these challenges, several survey respondents mentioned unfavourable foreign exchange rates (28%), increasing transportation costs (12%), and changes to minimum wage (12%). In particular, when asked about economic factors specifically, 84% of respondents reported that exchange rates have had a negative impact on their company in recent years. The declining Canadian dollar has resulted in significant costs increases for imported goods. Company respondents also stated regulatory compliance (e.g., safety standards, health regulations, packaging guidelines) as another factor contributing to increasing their cost of doing business in Canada.

Further, given the retailer landscape in Canada, FCP manufacturers may be constrained to absorb the majority of these cost increases as passing along production cost increases to retailers appears to be difficult. When asked about their experience trying to present a price increase for one of their products to a customer, many company respondents experienced major pushback from retailers including delays in accepting these increases (17%) — notably through retailers asking for specific breakdown of input cost increases — while other respondents were able to obtain only partial increases (39%) or were simply denied increases completely (39%). Specifically, when asked qualitatively about their experiences in passing along cost increases to retailers, respondents explained:

- “[cost increases were] not accepted at certain retailers. The cost increases were either out right rejected by the retailers or unauthorized deductions to get back to original net price were made. Where cost increase was rejected, our brands were removed from store shelves for a certain timeframe.”

- *“It is getting very difficult to take price increases. The last time we tried to take price increases was 2016 and we were able to take only partial increases. Since then it has been almost impossible to take price increases based on very restrictive criteria from customers. The information they require regarding formulations is often highly confidential.”*

4.1 Dim prospects for future profitability

The costs increases have an impact on FCP manufacturers’ potential for growth in profitability. Overall, gross profit margins among all survey participants have remained constant on average over the past three years (**Table 4.4**).³⁷ However, the negative pressures on margins have been greater for food manufacturers than for other manufacturers. In addition to trade spend being more costly for this group (as discussed in the previous section), the costs of goods sold are also far higher for this subset of firms. As a result, gross profits of food manufacturers have grown at a slower pace than gross profits for non-food manufacturers.

Table 4.4
Change in Gross Profit Margin, 2017 versus 2015

Subset of Firms	Percentage Point Change 2017 vs. 2015
All firms	-0.07 pts
Food/ Beverage/ Animal Food	-0.49 pts
HaBA / OTC / Household Cleaning / Paper Goods / GM	+0.81 pts

Notes:

[1] Table includes data from 19 companies with sufficient data from 2015 to 2017 (14 food manufacturers, 5 non-food manufacturers).

[2] Gross profit margin = Gross profit / Gross sales

Source: FCPC Industry Sustainability Survey, 2018.

³⁷ Gross profit margins are computed by dividing gross profit (defined as net sales minus COGS) by gross sales. Net sales are defined as gross sales less the sum of trade spend, customer marketing, and trade fines and fees.

Table 4.5
Average Net Profit Margin for the Canadian Food Manufacturing Sector, 2014 – 2015

Year	Net Profit Margin
2014	4.6 %
2015	3.7 %
2016	4.8 %
2017	4.4 %

Note:

[1] The table presents the yearly average pre-tax net profit margin for the food manufacturing sector in Canada.

Source: Statistics Canada; Meyer-Robinson, Robert. *Canadian Industrial Outlook: Food Manufacturing—Summer 2018*. Ottawa: The Conference Board of Canada, 2018, p.1.

According to a recent report by the Conference Board of Canada, net profit margins for food manufacturers (which also take into account operating costs) have remained relatively constant in recent years (**Table 4.5**). On average, profit margins for food manufacturers (4.4%) were among the lowest across Canadian manufacturing sectors in 2017. In particular, they were lower than the margins of motor vehicle parts, paper, aerospace, and textile and apparel.³⁸

5. Challenge #5: The number of full-time employees among survey respondents in the FCP industry has been decreasing

Manufacturing jobs have been declining for decades in developed countries. Between 1998 and 2014, the number of manufacturing jobs declined by 23% in France, 9% in Germany, 25% in Japan, 40% in the UK, 23% in the US, and 19% in Canada — while increasing by 49% in Brazil and 16% in Mexico.⁹ Still, manufacturing jobs are a significant source of employment, representing 9.5% of Canadian jobs in 2015.³⁹

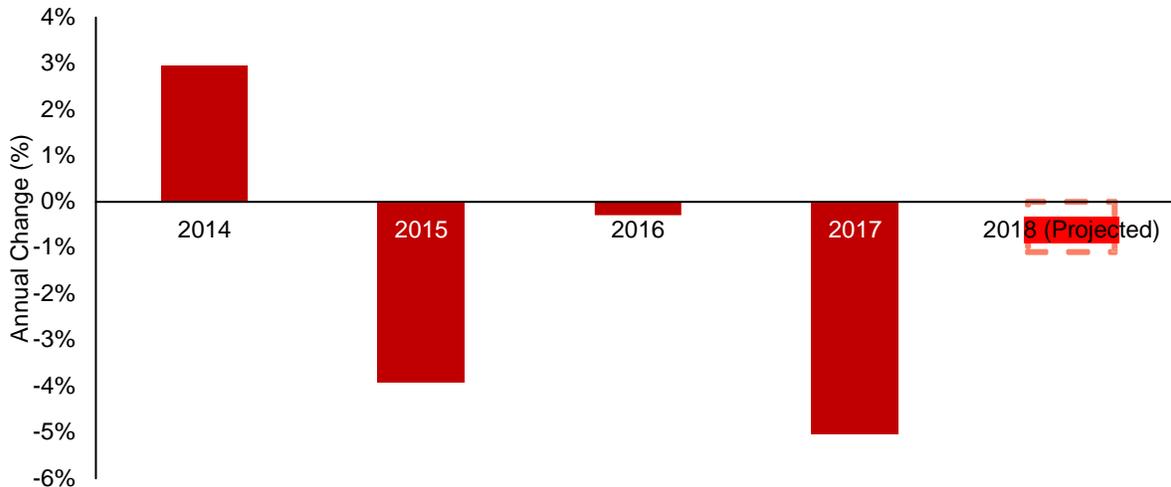
Given this global decline, it is not surprising to observe a downward trend in the number of full-time employees among company respondents (**Figure 5.1**). For participants who provided data across all years, this number shrunk by 7.3% between 2013 and 2017 despite a spike in 2014.

³⁸ See Statistics Canada; Meyer-Robinson, Robert. *Canadian Industrial Outlook: Food Manufacturing—Summer 2018*. Ottawa: The Conference Board of Canada, 2018, Chart 2, p.9.

³⁹ See House of Commons Standing Committee on Industry, Science and Technology (2017), *The Canadian Manufacturing Sector: Urgent Need to Adapt*, http://publications.gc.ca/collections/collection_2017/parl/x39-1/XC39-1-1-421-6-eng.pdf

Assuming this trend was the same for the entire FCP industry, this would equate to a loss of up to 22,000 jobs.⁴⁰

Figure 5.1
Annual Change in the Number of Full-time Employees among Respondents, 2014 – 2018



Note: The chart was created from the 20 survey respondents who provided data across all years

Several reported explanations for the decrease in the number of full-time employees include labour relocation or outsourcing certain operations outside of Canada (20%). A smaller portion of respondents (12%) explained this decline by increased efficiency and automation in certain production processes (internal economies of scale). Indeed, in recent years, average output per worker has increased in Canadian food manufacturing.⁴¹ Other plausible explanations for the decrease in the number of full-time employees could include firms relying more heavily on part-time workers or contract workers.

Costs of operations are expenses related to the operation, maintenance, and day-to-day administration of the company.⁴² Among survey respondents, the total cost of operations

⁴⁰ This extrapolation assumes that the 300,000 jobs in the FCP manufacturing sector are full-time positions. According to Statistics Canada, the majority of jobs in the manufacturing sector are full-time positions. See Statistics Canada, “Manufacturing”, available online at: <https://www150.statcan.gc.ca/n1/pub/11-402-x/2011000/chap/man-fab/man-fab-eng.htm>, accessed on October 2, 2018.

⁴¹ See Meyer-Robinson, Robert. *Canadian Industrial Outlook: Food Manufacturing—Summer 2018*. Ottawa: The Conference Board of Canada, 2018, Chart 2, p.11.

⁴² Total costs of operations (or total operating costs) include the costs of warehousing, logistics & distribution, consumer marketing, sales and sales support, and corporate costs. These include warehouse-related direct labour costs as well as indirect labour costs (e.g., salaries of employees in sales, marketing, and merchandising and employees related to corporate offices, finance, HR, IT, and procurement).

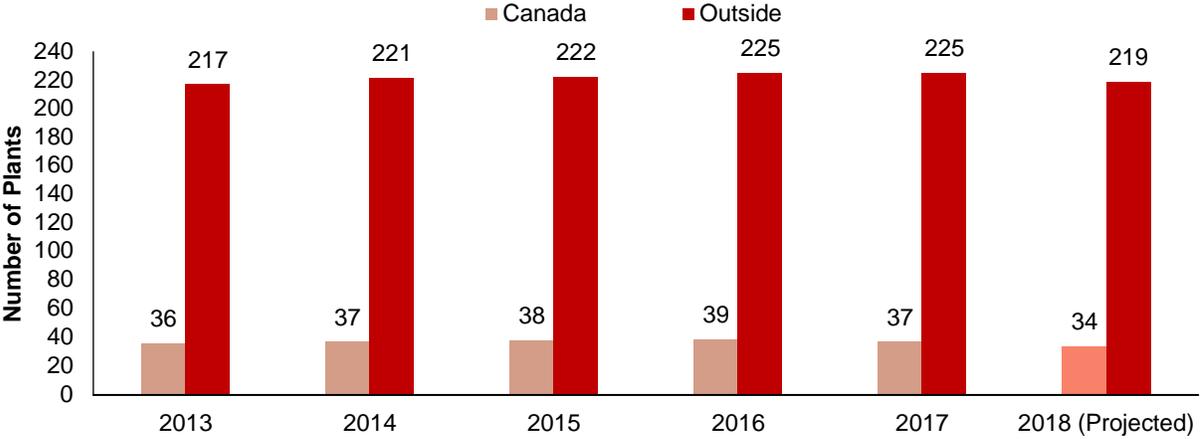
decreased slightly between 2013 and 2017, which may be linked to workforce reductions (or shifts in workforce composition) and increased automation.

6. Challenge #6: Manufacturing capabilities appear to have remained constant both within and outside of Canada

Consistent with other industry health indicators, manufacturing capabilities in Canada do not point to any sign of significant industry growth in Canada. The number of Canadian plants has remained approximately the same over the past few years, and capital investments appear to relate mostly to maintaining or improving/expanding existing plants.

Among company respondents, over the past five years, there has been little to no change in the total number of company-owned plants used to manufacture products sold in Canada. Among the respondents who provided data for all years, the reported number of plants in Canada increased marginally from 36 in 2013 to 37 in 2017 (Figure 6.1).

Figure 6.1
Number of Company-owned Plants Used to Manufacture Products Sold in Canada, 2013 – 2018



Note: Chart includes data from 22 companies with sufficient data from 2013 to 2017.
Source: FCPC Sustainability Survey, 2018.

As mentioned before, manufacturers are not shifting production to Canada, despite (arguably) favourable economic conditions (i.e., USD-CAD exchange rate). Domestic plants produce less than half of all domestic sales. The share of sales of products manufactured in Canada has remained constant over the years at approximately 45% of Canadian sales (Table 6.2).

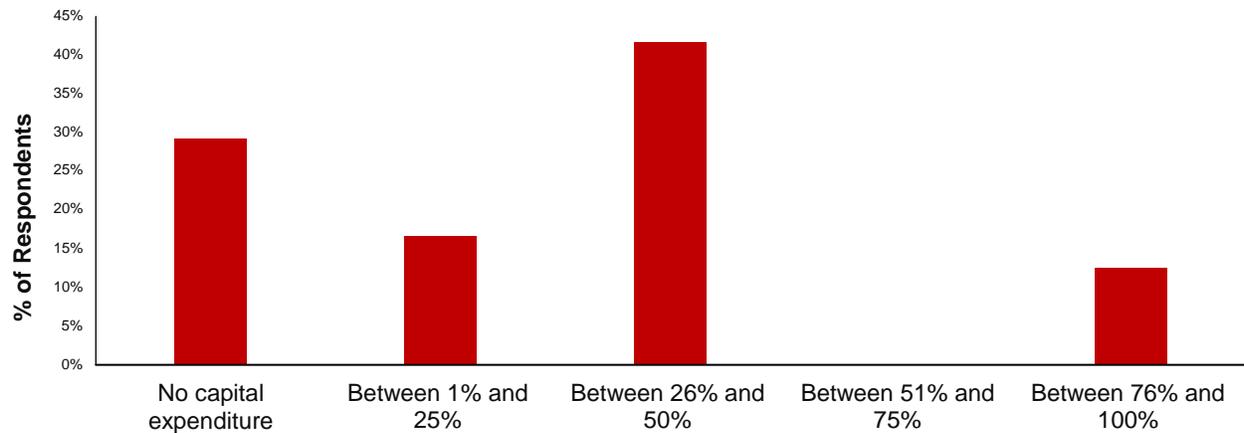
Table 6.2
Percentage of Canadian Sales Corresponding to
Products Manufactured in Canada, 2013 – 2018

Year	Percentage of Sales Manufactured in Canada
2013	44.9%
2014	46.0%
2015	45.7%
2016	46.0%
2017	44.4%
2018 (<i>Projected</i>)	45.2%

Note: In each year, percentages are computed from all respondents who provided data on this topic. In 2013, 2014, and 2018, the sample size is 19 respondents, whereas in 2015-2017, the sample size is 21 respondents.
Source: FCPC Sustainability Survey, 2018.

Although survey results reveal that the total number of domestic plants and the overall proportion of domestic production has been constant in recent years, the majority of firms with plants located in Canada reported capital investments allocated either towards maintaining operations or towards expanding manufacturing capabilities in Canada over the past five years. Somewhat surprisingly, 71% of respondents reported having invested *some* capital in expanding manufacturing capabilities in Canada within the last five years (**Figure 6.3**). Given the stable number of manufacturing plants, these investments were likely related to improving/expanding existing manufacturing plants.

Figure 6.3
Percentage of Capital Expenditure (CAPEX) Related to Expansion Investments
over the Past Five Years



Note: Chart includes data from the 24 companies with sufficient data.
Source: FCPC Sustainability Survey, 2018.

Some company respondents have not reported any capital expenditure in either maintaining or expanding operations in Canada. The current favorable situation in terms of exchange rate should be favorable to domestic investments. Therefore, an absence of investment could illustrate a lack of confidence in the Canadian market or a desire to consolidate activities abroad. A few respondents mentioned looking for co-manufacturing/co-packing opportunities, namely because “the efficiencies gained by manufacturing in Canada are small”. Another survey respondent explained that “the cost to produce in Canada is typically higher than the US due to scale, the regulatory environment (i.e., corporate taxes and employer taxes) and wage expectations.”

C. These Challenges Pose Serious Threats to the Future Sustainability of the Food, Beverage, and Consumer Products Industry

The results of this study reveal that the food, beverage, and consumer products manufacturing sector — a critical contributor to Canadian jobs and to the Canadian economy — is under considerable stress. Growth in costs, which has accelerated in recent years, has squeezed margins. Barriers to innovation, such as the increasing costs of trade spend, have dampened the development and manufacturing of new products in Canada. Additional challenges such as the declining Canadian dollar, minimum wage regulations, and the consolidation of retailers are also important concerns for surveyed industry participants. Finally, onerous compliance costs and the burden of new regulations (increasing in both number and complexity) also limit investment

potential in Canada for the industry. These barriers, which are discussed in our qualitative analysis, are also confirmed by other studies.⁴³

Critically, multinational manufacturers produce the majority of products sold on store shelves.⁴⁴ These manufacturers examine the relative attractiveness of many markets as they choose to invest (e.g., locate new plants, invest in current plants, and create R&D centres). The uncertainty and the recent relatively poor performance of the Canadian industry puts Canada at a disadvantage when multinational companies consider where to make investments. Recent decisions by companies such as Heinz and Campbell to shut down manufacturing plants in Canada show the potential impact that these uncertain conditions may have.⁴⁵

According to a recent internal FCPC survey, over 65% of multinational respondents reported that their Canadian profit margins were considerably lower than their U.S. or international profit margins. Moreover, the Canadian segment has experienced diminished ROI over the past years. The Canadian market profit margins are dilutive to overall company margins. Future investment in Canada is being questioned by multinational corporations due to trade consolidation, cost to serve, and weakening currency.⁴⁶

Given existing pressures on margins, the business case for investing in Canadian food, beverage, and consumer products manufacturing is not readily apparent. Although the food, beverage, and consumer products manufacturing sector is critically important to the Canadian economy and has untapped potential for growth, our data and analysis clearly show an industry at risk. Without changes to the business environment, the FCP industry may diminish substantially — putting Canadian jobs and the economy at risk.

⁴³ See The Canadian Chamber of Commerce, “Death by 130,000 Cuts: Improving Canada’s Regulatory Competitiveness”, May 2018, available online at: http://www.chamber.ca/advocacy/regulate-smarter-toolkit/DRAFT_DeathBy130000Cuts_ImprovingCanadasRegulatoryCompetitiveness.pdf; Advisor Council on Economic Growth, “Unleashing the Growth Potential of Key Sectors”, February 6, 2017, available online at: <https://www.budget.gc.ca/aceg-ccce/pdf/key-sectors-secteurs-cles-eng.pdf>

⁴⁴ Only 11.5% of survey respondents are Canadian owned and Canadian operated companies. The large majority are U.S. owned or internationally owned.

⁴⁵ Heinz closed a factory in June 2014 in Ontario. In January 2018, Campbell announced the closure of one of its factories in Toronto. See CBC, “Heinz closes Leamington plant, 740 people out of work”, 2014, available at <https://www.cbc.ca/news/canada/windsor/heinz-closes-leamington-plant-740-people-out-of-work-1.2426608>. See also Campbell News Release, “Campbell Announces Plans to Improve Operational Efficiency of Its North American Thermal Supply Chain Network; Company to End Manufacturing at Toronto Plant”, January 24, 2018, available online at: <http://investor.campbellsoupcompany.com/phoenix.zhtml?c=88650&p=irol-newsArticle&ID=2328225>.

⁴⁶ See Internal FCPC survey, September 2018.