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Food Industry 2001 Review

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Summary Points

- Food manufacturing enjoyed a very good year in 2001. Sales increased at a strong pace despite the poorer economic conditions in Canada.
- Food retail sales also saw solid increases.
- Both food manufacturers and food retailers increased their share of overall manufacturing and retailing during 2001.
- Price increases were hard to attain for both manufacturers and retailers during 2001. At retail, grocery prices actually declined significantly after July. At wholesale, food manufacturers were unable to push along increased prices.
- Profits were excellent for both manufacturers and retailers last year. Both managed to get operating costs under even greater control.
- Food manufacturers continue to prepare for the future by aggressively spending and investing in capital and equipment.

During the latter part of the 1990's when much of the economy, particularly the technology sector, was booming the food industry appeared stodgy at best. Market analysts were clamouring for anything that would boost food industry stocks. The calls were typically for mergers and acquisitions. The fact is, however, in slower economic periods the food industry continues to trudge along at relatively the same speed it did during the good times. This, of course, should not be surprising to anyone. In fact, the past year provided a good example of the food industry's resilience and strength during relatively poor economic periods.

Food Manufacturer's Gain Share

Throughout the 1990's the food manufacturing industry lost share of total manufacturing sales. It is apparent now that 2001 is going to be the first year that the food industry has gained sales share in many years. The gain in share is testimony both to the fact that Canada is enduring slower economic growth and that the food industry is largely immune from those forces.

From January through October of 2001, the food manufacturing sector grew by nearly 7% while total manufacturing (including food), declined by 4.25%. The growth in food and the decline in overall manufacturing are both very significant and surprisingly large numbers, especially since they are in opposite directions. The George Morris Centre estimates that for the year, Canadian food manufacturing sales will total $62.3 billion. That represents an increase of 6.5% over 2000. That sales figure, in combination with the estimated sales for all of manufacturing, means that food took a 12% share of all manufacturing sales. That compares to less than 11% in 2000 and more than 13% in 1993. The following graph (figure 1) shows 2001 sales through October compared with 2000 sales and the five year average . Figure 2 shows the food industry's share of total manufacturing sales.

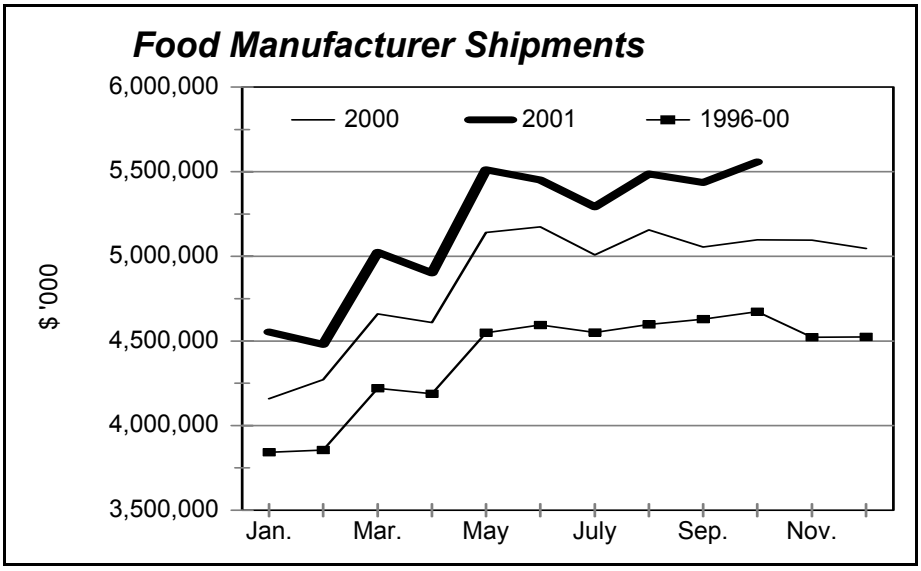

Figure 1

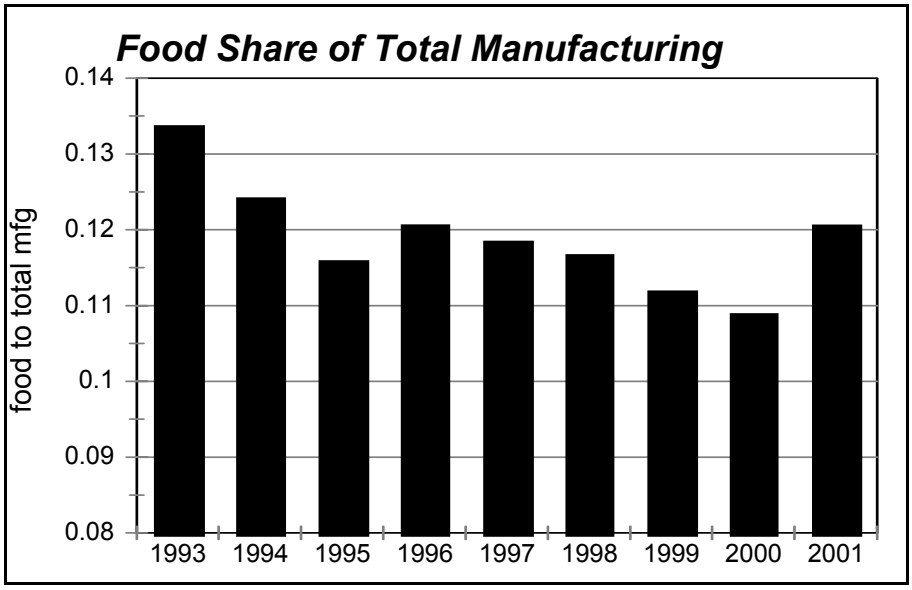

Figure 2

Food retailers also enjoyed a relatively strong 2001. Statistics Canada sales data is only available through September, but for the first three quarters of 2001, grocery sales increased by 4.3%. Assuming typical sales in the final quarter, the George Morris Centre is estimating 2001 sales of $58.9 billion compared to $56.6 in 2000.

The grocery sales share of total retail sales in Canada also declined through the 1990's. The relatively solid increase in sales during 2001, coupled with a more modest increase in all retail sales meant that grocery share increased. During 2001 it is likely that grocery sales comprised about 21% of all retail sales. That compares to 20.4% in 2000 and over 24% in 1993. The following graph (figure 3) shows supermarket sales estimated for 2001 compared to annual sales for the previous eight years.

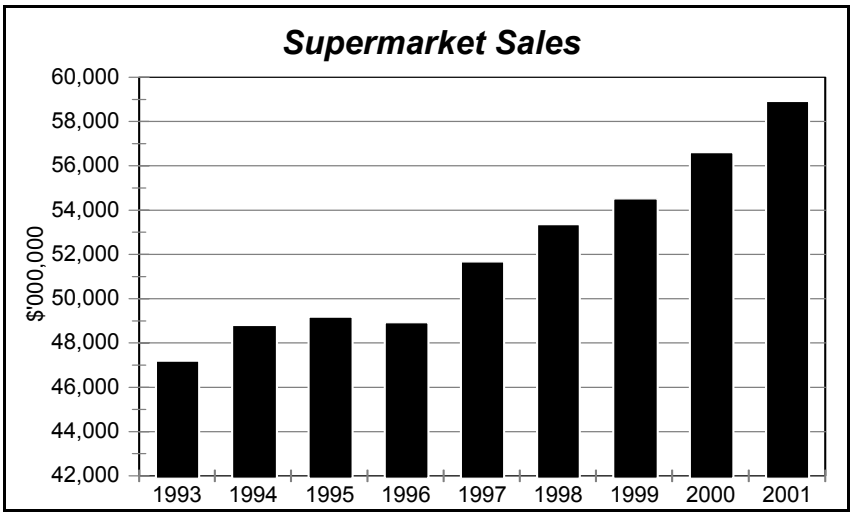

Figure 3

Based on the performance of prices, it appears that supermarkets are making sales gains via volume as opposed to price hikes. This is an important piece of information given the consolidation that has taken place in the industry during the past three years. There had been concern, as the grocery sector moved into fewer and fewer hands, about the impact on competition and prices. The evidence so far indicates that this is a non-issue.

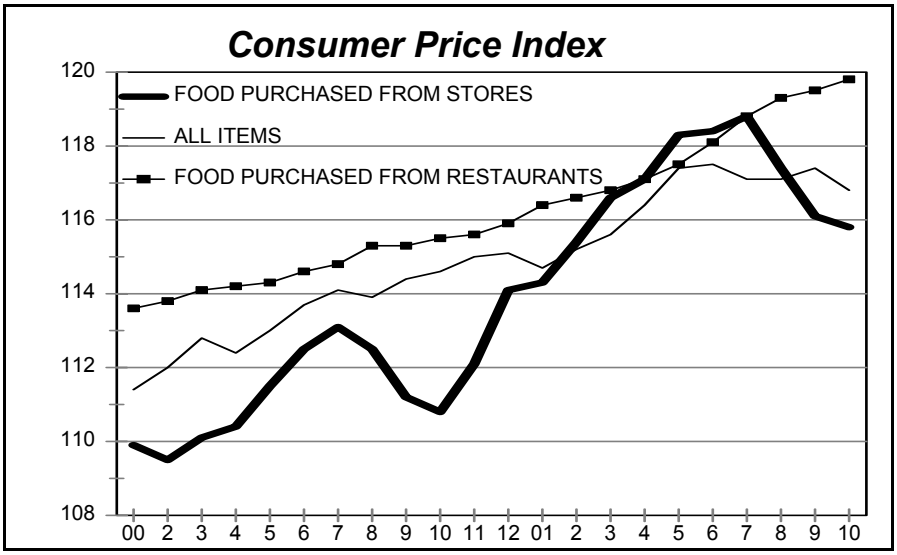

Figure 4

The consumer price index for food purchased from stores has been declining fairly dramatically since July 2001. That stands in contrast to price gains at restaurants. The graph on figure 4 shows the performance of the consumer price index for all items, food purchased from stores, and food purchased from restaurants through October 2001 (latest data). Supermarkets led the entire CPI downward.

For their part, food manufacturers also seem to be having a difficult time attaining price increases. This is testimony to both the degree of competition within food manufacturing and the challenge of passing along price increases to a strong retailer buying sector. Figure 5 shows the wholesale price index for prices between manufacturers and retailers.

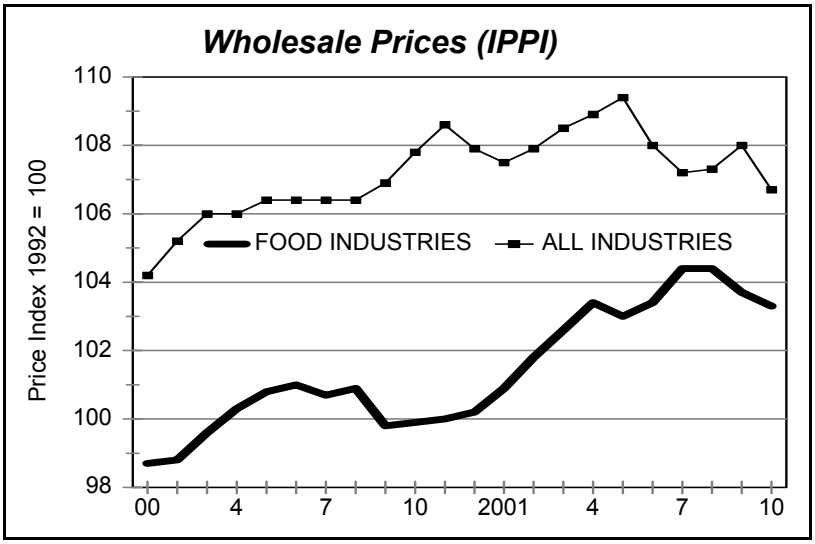

Figure 5

Profits are Strong

Food manufacturers enjoyed an excellent year in 2001 with regard to profitability. During the first three quarters of the year, (latest data available) profits were up by 27% compared to the first three months of 2000. The best quarter was the second when profits surged ahead by 41%. During the first three quarters of 2001, net margins after tax averaged approximately 4%. That compares to a 3% average net margin during the first three months of 2000 and 1999. The graph on figure 6 compares net margins for manufacturers and distributors.

With regard to distributors, (statistically defined as food and beverage retailers and food wholesalers), their profitability pattern performed according to seasonal norms. Profitability tends to rise throughout the year to hit annual highs in the fourth quarter. Last year was shaping up to be no exception. Overall profitability for distributors was very good during the first three quarters of 2001. Cumulative profit for the three quarters was up by 13% compared to the same period in 2000. Third quarter net profits were particularly strong compared to the previous year.

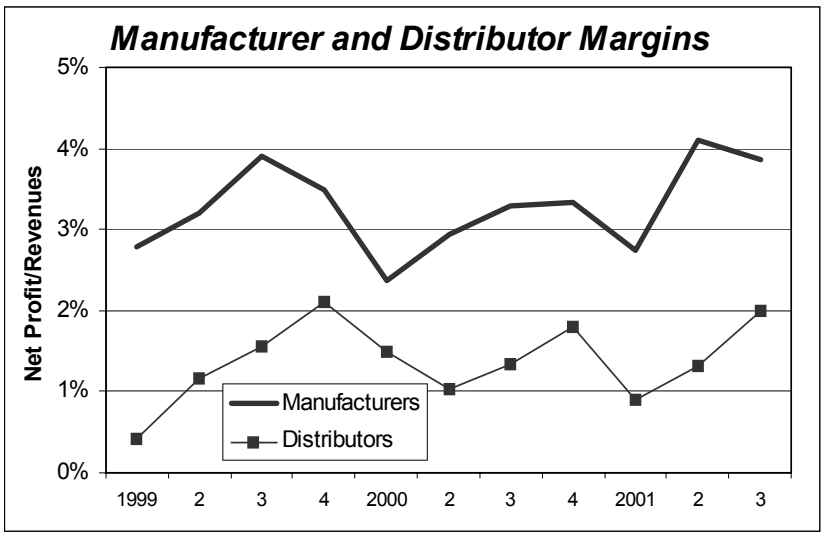

Figure 6

Overall for 1999 through September 2001, distributors saw net margins average approximately 1%. Over the same period of time, food manufacturer margins have averaged about 3%. It is notable that since 1999, manufacturer operating expenditures (which included COGS) have stayed around 94-95% of revenues. Distributors, on the other hand, have managed to shave their expenses as a share of revenues from about 97-98% in 1999 to 96-97% in 2001.

It is also interesting to examine the relative increases in capital investment occurring in the food industry. The following graph shows capital expenditure as a percentage of total revenues for both food manufacturers and distributors. As can be seen, prior to 2001 manufacturers and distributors were investing at relatively similar rates. During 2001, however, manufacturers significantly increased their rate of capital investment while distributors decreased their investment relative to revenues.

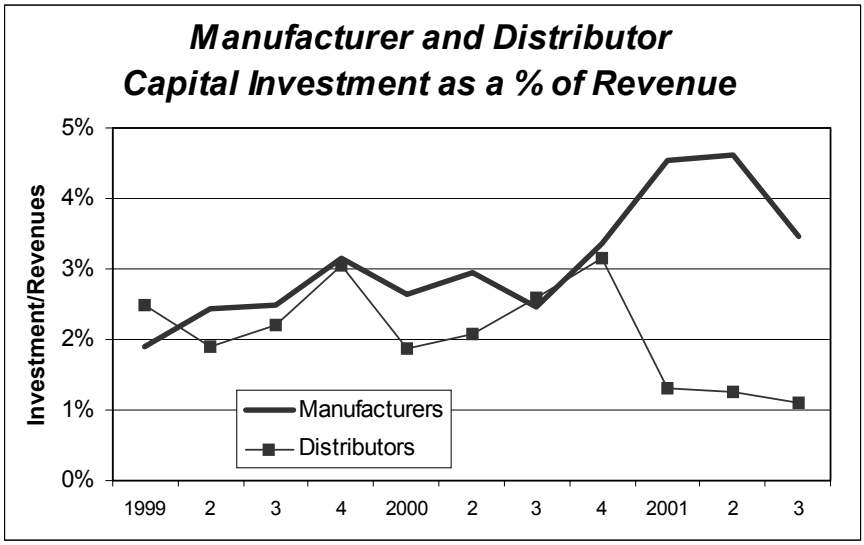

Figure 7

While future profits are never guaranteed, one way to gain advantage is to re-invest profits aggressively. That appears to be the tactic that manufacturers are using for their future.

Comment

The performance of the Canadian food industry during 2001, is consistent with the forecasts and analysis on the industry that the George Morris Centre conducted during the summer of 2001. The George Morris Centre published two reports: Comparative Analysis of Productivity in Agrifood and other Industries in Canada and; Comparative Analysis of Productivity and Competitiveness in Agrifood processing in Canada and the United States.

Those studies raised serious questions regarding the comparative competitiveness of the Canadian industry relative to the United States. At the same time, however, the studies noted forecast that the food industry would grow relative to other industries. Essentially the George Morris Centre pointed out that the food industry might not be as exciting as the tech sector, but it may be a better investment in the long run.

A similar version of this article appeared in the January 2002 issue of the George Morris Centre's Grocery Trade Review. If you would like a sample copy of Grocery Trade Review or if you would like to subscribe, please visit our website at georgemorris.org or call Kevin Grier at 519-822-3929x202