GEORGE MORRIS CENTRE

Heinz and Kellogg Plant Closures: What Direction for Canada's Food Manufacturing Competitiveness?

Bob Seguin
Executive Director

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INTRODUCTION

In the past number of weeks, two major long standing food manufacturing companies in Canada- HJ Heinz Canada and Kellogg's Canada- closed two well-known processed food manufacturing facilities in Ontario (Leamington and London respectively). Both companies indicated a number of reasons for the closures and noted their efforts to provide additional assistance to the affected employees and communities.

Media commentators immediately picked up on the economic, financial, human, and policy impacts of these developments. A number of commentators quickly identified a variety of reasons for the closures- single factors (e.g. exchange rates), market factors, new owners, multiple input cost issues, age of facility, regulatory issues. This was matched with an equally wide range of possible responses by industry and government. Underlying the public comments were the implications for the longer term viability of Canada's food manufacturing industry and for possible public and private policies or actions needed to change or revive this industry. The timing of the closure announcements was juxtaposed with strong statements of the growth potential in national or regional food manufacturing by senior governments across Canada.

This report outlines the scale of this national industry which underlines its importance as a significant economic driver in its own right, and as a critical segment of Canada's agri-food sector, as well as the broader economy. The current and future competitive challenges include the dilemma of matching growth opportunities with legacy issues within the industry. These competitive challenges and legacy issues apply equally to the regulatory contexts of this national industry. Finally, the report identifies a series of market and policy responses which acknowledge the transition challenges facing this industry across Canada, but also clear opportunities for Canadian food manufacturing to meet these challenges. A renewed commitment to industry leadership, acceptance of the competitive challenges and significant leadership roles in moving away from status quo market and policy responses-and all the difficulties that implies-are all key to future growth and prosperity for this industry-nationally and regionally.

FOOD MANUFACTURING IN CANADA

It is acknowledged that Canada's agri-food sector is a key component of national, provincial and regional economies within Canada. Canada's food manufacturing industry is a critical part of the sector. According to Agriculture and Agri-Food Canada for 2011:

- Food and beverage shipments were valued at $92.8 Billion;
- Food and beverage industry accounted for 14.5% of total manufacturing activity in Canada, second to the transportation equipment industry;
- Food and beverage employment in Canada exceeded 280,000, larger than the transportation equipment industry;

- Food and beverage manufacturing exists in all provinces, but approximately 55% of all establishments were in Ontario and Quebec;
- Over 84% of Canadian food and beverage manufacturing establishments had less than 50 employees, but accounted for 17% of total industry shipments;
- In contrast, 3% of national food and beverage manufacturing establishments (those over200 employees) accounted for approximately 50% of industry shipments;
- Approximately 25% of food and beverage shipment were exported-with the largest share of exports moving to the United States;
- Profit margins in food and beverage manufacturing varied annually but remained relatively stable, but have weakened slightly recently; and,
- Investment in capital stock in food processing stock in Canada hovered around $1.7 Billion in constant dollars annually, almost matching estimated replacement needs.[1]

This quick recap of key statistics provides a sense of the scale, national scope and relative stability of this industry. These strengths reinforce the recent public and private sector ambitions for this industry with its attendant positive impacts on other supplier industries- primary production, packaging, machinery, logistics-and on the demand side (food retailers, foodservice firms) These statistics also do not address the number of plant opening, expansions or closures over the past decade. The ongoing bipolar trends of plant consolidations and plant expansions do not always attract detailed public attention. These are trends which the Food Processors of Canada are closely monitoring, among others,[2] and gaining wider awareness. It is anticipated the downward trends in secondary food processing balance of trade over the last decade[3] will further increase concerns about long term industry viability.

These key statistics cannot sufficiently provide detailed insights into the legacy of this industry across Canada. This industry has evolved with the growth of the country adapting to very changed marketplaces-partially due to the unique demands of two World War and significant population growth and diversity over the past decades. These consumer developments have led to: significant shifts in plant and product technologies; in the skills sets required; tremendous and continuing consumer taste changes, domestically and internationally; expansion and consolidation of various segments of the industry; and the juxtaposition of aging facilities with new food demands varying across the country. The significant increase in demand for processed organic foods, new local food demands, or even new products such as gluten-free foods, or Greek yogurts, are all examples of a dynamic food sector. But, making the transformation from one industry model to another cannot be smooth or costless when existing legacy facilities (once central to major firms and communities) and accompanying legislation form a significant part of the current industry.

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[1] 2013 An Overview of the Canadian Agriculture and Agri-Food System, Agriculture and Agri-Food Canada, Public Works and Government Services Canada, Ottawa. May 2013. P 103-122
[2] Food Processors of Canada website 2013
[3] Dr. D Hedley, "The State of Canada's Processed Food Sector: Trade Balance", Canadian Agri-Food Policy Institute, Ottawa. November 2012

A number of Premiers, as well as the Government of Canada, have identified sustained growth in this segment of the national agri-food sector as a key economic prosperity challenge. This extends to renewed growth in certain domestic product markets, even in local markets, and increasingly in global market opportunities reflecting improvements in personal incomes in new emerging economy markets. Unfortunately the identification of the opportunities for this industry has not been matched by the full details of the private and public sector strategies needed to successively fulfil these public, and private, sector ambitions.

FUTURE CHALLENGES TO THE SUSTAINED GROWTH OF CANADA'S FOOD MANUFACTURING

For many proponents of Canada's food manufacturing industry growth and prosperity the clear focus is on future market opportunities-domestic and international. But, the historical legacy and evolution of this industry-scale, age, supply chain linkages and the regulatory context-all shape the capacity to adapt and transform this industry. The existing industry legislation and regulation provides legal protection for existing industry assets and practices and, at times, binding constraints on industry market innovations, expansions and responsiveness. Market opportunities and the industry legacy provide the necessary contexts for the significant future challenges for Canada's food manufacturing industry.

These key industry challenges can be summarized as:

- Increased domestic and international competition for food manufacturing by new products, technologies, new market players, and from competitors from new international jurisdictions;
- Continued dramatic shifts in consumer tastes and preferences domestically and internationally;
- Aging industry infrastructure in many of the traditional industry markets and competitive shifts in availability of talent (plant and management) creating new challenges to invest, re-invest or disinvest in the industry;
- Increased competition for capital, land, labour (including talent) and technology between industry sectors, within the industry sector, and between jurisdiction;
- Continued consolidation of facilities in certain markets (primary processing in some cases) and expansions into new technologies or markets (craft brewers, different food packaging as examples);
- Need to modernize and adapt the existing national and provincial legislative and regulatory environments for the Canadian food manufacturing to better reflect these ongoing market developments , and increased competition; and,
- Recognition of the evolving roles of the public sectors in encouraging, or limiting, industry growth and prosperity over time.

These challenges and the demands on the industry signal the need to be adaptable, flexible, cost conscious, well managed, and prepared to take risks to be successful over time. The demands from consumers, retailers and foodservice firms do not reward extended periods of status quo activity and

investment. Within this context, the decisions regarding the Heinz Leamington and Kellogg London plant closures can be seen as part of a much wider set of industry challenges and opportunities. Segments of North American food processing are undergoing a long period of consolidation and market adjustment as can be seen in the recent Chapter 11 filing in late Fall 2013 by Allen's Inc.- one of the largest canned food processors in the United States

Across Canada in the same domestic and regulatory marketplace, a number of new firms or current industry competitors are making new investments, expansions and innovations. The 2011 announcement of the new Dr. Oetker facility in London, the expansions over the last decade in Western Canada in canola processing, or Premium Brands purchase of Piller Sausages & Delicatessens Ltd. or its purchase (and re-investment) in B.C. seafood processing, or the recent Oxford Frozen Foods $184 million investment in wild blueberry in New Brunswick are just examples of positive trends in this national industry.

The capacity of the private and public sectors to provide the appropriate market and policy responses to support and sustain such growth opportunities will determine the future directions of the Canadian food manufacturing industry. In choosing an industry direction involving sustained growth, prosperity and greater manufactured food exports will require market and policy responses that go beyond the status quo.

MARKET AND POLICY RESPONSES FOR CANADA'S FOOD MANUFACTURING INDUSTRY

For many industry observers, the closures of a number of food manufacturing plants in the past decade, including the Heinz and Kellogg plant closures in the past month, all point to reduced competitiveness in the domestic food manufacturing industry. This view has merit. But, as noted above, it misses the market nuances of expanded investments, exports, internal and external market developments. The market and policy responses by private and public sectors require more subtlety than simply lowering all costs, or eliminating all regulatory constraints.

These market and policy responses must operate within the dynamic marketplace-for food manufacturers, and throughout their value chain. To expand the beneficial impacts of the possible responses, these must apply to growers, suppliers and retail/food service industries. These market and policy response must also address longer term capital, human resources infrastructure and regulatory reforms in order to sustain the desired growth and prosperity in this industry.

The following suggested market and policy responses build upon these efforts. However, these market and policy responses also emphasize the need to initiate, complete and ensure substantive results in these key areas.

1. The primary focus of any significant market or policy responses must be on obtaining new domestic and foreign investments, and re-investments in this industry. Entrepreneurial growth

and investment s (re-investments) in scale and new technologies must be complementary priorities.

2. New investments in developing new and needed labour pools for a successful food manufacturing industry must be encouraged and spurred. The industry's past successes using traditional sources in rural and urban Canada are not sustainable. New investments in seeking both domestic and foreign labour as well as improved management expertise (for a much more competitive marketplace) must be priorities in order to successfully compete.
3. Increased competition within Canada's domestic markets as well as its traditional export markets has to be the factor in private and public sector responses for future industry growth. This means the need to learn from competitors in these marketplaces including the public policy and regulatory supports available to these current and new competitors.
4. Regulatory reform must focus beyond just removing unneeded or outdated regulations. The competitive impacts within a dynamic marketplace must become a critical factor in the regulatory choices and processes for implementation. Improved measures of results, impacts and effectiveness must become standard if the domestic industry is to adapt while sustaining public demands for different regulatory standards.
5. Public and private research and private sector innovations in this industry must become better coordinated. It is important to build upon past research successes, and to seek more innovative market and policy responses needed to match Canada's innovation investments and successes (real results in the marketplace) with its competitors.

These efforts, combined with a greater focus of public investment marketing efforts to better secure expanded domestic and foreign investments in this industry, should lead to the desired results of more sustained economic growth and prosperity in this industry. These expanded investment marketing efforts must also learn from what has not been as successful and what disinvestments are occurring, and why. The competition in food manufacturing market is intense. The competition for capital among sub-national jurisdictions is as intense and innovative as the goods markets.

The demise of Canada's food manufacturing industry is not a "done deal". This industry can fulfil the many public and private sector ambitions for it. But, key changes have to be made, new investments won, far greater competitiveness in public policy as well as in private markets are required. The closures of key Canadian food manufacturers in the past years and months are the results of a number of past market and public policy developments. It cannot be expected that the significant transitions within the industry will be costless, or easily accepted.

However, not learning from these dis-investments and the potential to re-energize the industry and individual firms or new entrants would be the real misfortune for this industry. Leadership by private and public sectors can provide the necessary capacity to work through industry transitions, asset reallocations, new product innovations and establishing a new foundation for the Canadian food industry and its regulatory contexts. Learning from these closures, from the new competitors and the shifts by consumers can continue the industry onto the growth and prosperity path desired by all participants.