

The Atkins Diet and Consumer Indulgence Drives Dairy Sales

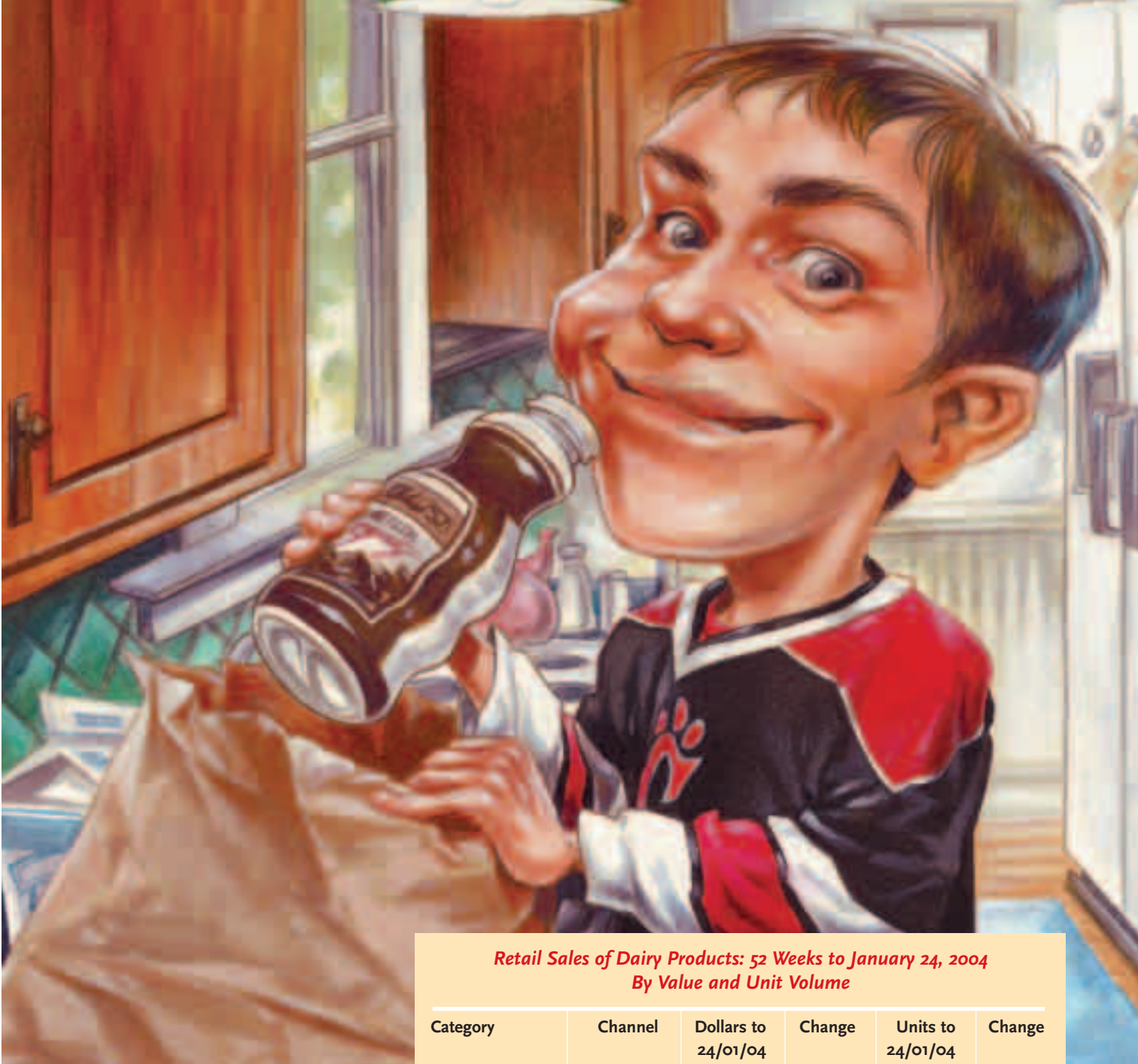
BY DOUG BURN

# Trading UP

**C**anadians shrugged off concerns about fat in 2003 and went for second helpings of dairy products. Perhaps it was trans fat avoidance that prompted them to switch from margarine to butter or the Atkins diet that caused the surge in sales of eggs and cheese. Yogurt, on the other hand, enjoyed yet another year of exceptional sales gains. Consumers also sent a mixed message in the fluid category with skim milk making slow but steady inroads on its two per cent and three per cent rivals while 18 per cent table cream lapped the

track. Dieticians, however, may be pleased to see an apparent gain for two per cent milk at the expense of soft drinks due to the popularity of single serve plastic bottles of flavoured milks. While overall fluid milk sales were flat in 2003, retail sales of the upstart milk alternatives – soy and rice drinks – approached \$100 million or five per cent of fluid milk sales in the grocery channel. The one constant in all the categories was a willingness among consumers to trade up to value-added products.

Processors are also paying a premium for milk but it's not a matter of choice. In December, the Canadian Dairy Commission (CDC) effectively hiked the price of industrial and fluid milk by 3.5 per cent by raising its support price for skim milk powder to \$5.40 per kg and that of butter to \$6.30. John Core, CDC chairman and a southwestern Ontario dairy farmer, explains that he was fulfilling the CDC's commitment to cover the cost of production of 50 per cent of Canadian producers by 2006. "The assumed processor margin will



**Retail Sales of Dairy Products: 52 Weeks to January 24, 2004  
By Value and Unit Volume**

Category	Channel	Dollars to 24/01/04	Change	Units to 24/01/04	Change
Fluid Milk	Grocery	\$1,773	+5%	588	+1%
Cream	Grocery	\$184	+8%	80	+5%
Soya Drinks	Grocery	\$84	+8%	26	+4%
Yogurt	Grocery	\$766	+14%	1,228	+14%
Cheddar Cheese	Grocery	\$567	+10%	104	+8%
Specialty Cheese	Grocery	\$183	+12%	41	+11%
Eggs	Grocery	\$478	+9%	212	+2%
Liquid Eggs	Grocery	\$11	+19%	5	+20%
Butter & Blends	G&MM&W	\$364	+3%	112	+0%
Margarine	G&MM&W	\$318	+1%	119	-2%
Ice Cream	G&MM&W	\$496	+3%	118	+2%

\* Grocery = National Grocery Banner excluding Newfoundland

\* G&MM&W = National Total Grocery & Mass Merchandisers & Warehouse + Club Stores

Source: ACNielsen MarketTrack 52 weeks to January 24, 2004

also increase by 3.5 per cent,” he adds.

The Canadian Restaurant and Foodservices Association (CRFA) protested that the new price of \$65 a hectolitre far exceeded the cost of production for many producers. Stephanie Jones, CRFA vice-president of food supply, notes, “We know from testimony to the federal agriculture committee that non-quota holding Canadian dairy producers can profitably export to the U.S. at \$44 per hectolitre. It defies the imagination when dairy producers say they need to charge over \$65

Photo: Craig McKay

per hectolitre when the same product is sold in Canada.”

Jones was referring to the short-lived Commercial Export Milk (CEM) program launched in August 2001, which allowed farmers to sell over-

quota milk for less than the industry-wide cost-of-production price if the milk was used to produce foods and beverages for export. In bulletin board auctions participating farmers bid the price down to \$44 a hectolitre. It was

ruled an export subsidy in December 2002 by the World Trade Organization (WTO) Appellate Body.

Canada's nascent dairy export sector was hard hit by the loss of the CEM program last year and the full effects won't be known until the end of 2004 because some orders made before the WTO ruling were allowed to ship in the first months of 2003. Domestic exports (foods and beverages produced from Canadian milk) had been growing by nine per cent annually to 2001 and in the next two years plummeted 24 per cent to \$328 million. It now appears that processors fulfilled their export contracts in 2003 by substituting imported milk proteins for domestic milk. Since 2001 re-exports of dairy foods have nearly tripled to \$39 million and all but 15 per cent of these re-exports were in the casein and casein product category.

#### INTERNAL TRADE BARRIERS

Now Canadian dairy processors are regrouping to tackle longstanding and emerging problems in their only remaining market – Canada. Six of our leading processors formed the Dairy Processors Association of Canada (DPAC) last December and have since added four more processors to give DPAC national coverage and reach.

Don Jarvis, DPAC's president, explains that the association's first objective is to reduce inter-provincial trade barriers for dairy products and increase the flexibility of this sector to accommodate industry consolidation and product innovation.

Industry consolidation and the centralization of purchasing by retail chains and foodservice distributors are creating new problems for the industry. Although processed fluid milk and dairy products, with the notable exception of coloured margarine, can freely move across provincial borders, the flow of raw milk to the dairies is allocated by the provincial milk marketing boards based on prior year sales. Jarvis notes that there are significant regulatory impediments for dairies seeking milk from producers across provincial

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borders. He notes that this is a particular concern for DPAC's members in Atlantic Canada where dairies prefer to supply the entire region from a single plant.

**BLIPS AND TRENDS**

The producers have proven themselves most accommodating of multi-year trends, such as the move to lower fat fluid milk or the decade-long rise in yogurt consumption. A sharp change in supply or demand, however, confounds the system. In 2002, for example, Ontario and Quebec instituted restrictive milk quotas and an exceptionally hot summer in Central Canada depleted production at the same time as cheese demand soared. The industry drew down inventories and the CDC was forced to import cheese from the U.S.

Something similar could happen in 2004 as ACNielsen reports a 10 to 12 per cent growth in retail sales of cheddar and specialty cheeses, respectively, for the 52 weeks ended January 24. Volume is up nine per cent to 135 million units, as compared to less than three per cent annual growth in consumption for specialty cheeses and flat growth for cheddar over the previous six years. Even the extended decline in processed cheese demand halted in 2003 as sales growth matched price increases.

Archie MacDonald suggests that cheese sales are benefiting from the conjunction of more effective generic advertising

**Canadian Balance of Trade in Dairy Products:  
1995 to 2003**

	1995	2003	CAGR* 2001 v. 1995	2003 v. 2001
	Millions	Millions	Per cent	Per cent
Domestic Exports <sup>(1)</sup>	\$ 261	\$ 328	+ 9%	- 24%
+ Re-Exports* <sup>(2)</sup>	\$ 3	\$ 39	+ 22%	+ 267%
= Total Exports	\$ 264	\$ 367	+ 9%	- 17%
+ Total Imports <sup>(3)</sup>	\$ 232	\$ 552	+ 15%	+ 1%
= Balance of Trade	+\$ 32	-\$ 185	- 17%	+ 76%

(1) Powdered milk & cream accounted for 2/3 of domestic export sales drop between 2001 & 2003  
 (2) Casein & casein products account for 85% of Re-Exports  
 (3) Cheese accounts for 40% of imports, whey and butter products for 30%  
 \* CAGR Compound Annual Growth Rate  
 Source: Statistics Canada: Merchandise Trade – HS Codes

at the same time as major processors are investing heavily in advertising for branded cheeses. MacDonald, who is director of economics and market research with the Dairy Farmers of Canada also notes that the "low carb/no carb phenomena has generated more change in diets than anything I can recall in the last 20 years."



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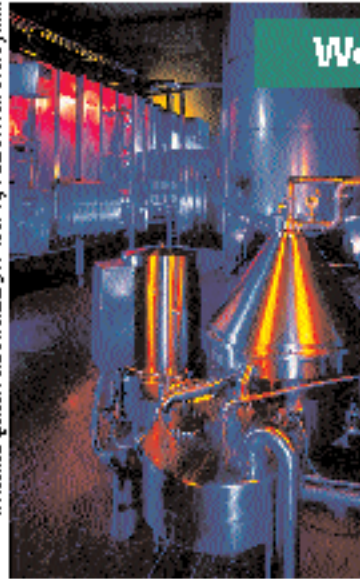
MacDonald also notes what may be an anomaly in the retail and food consumption data. While ACNielsen shows no growth in the volume of butter sold through supermarkets, consumption calculated from industry production net of beginning and ending stocks rose by almost five per cent in 2003 to 3.18 kgs per capita. "That's the first significant increase we've seen in quite some time," says MacDonald, "and if the sales aren't moving through the retail channels, they may be generated by the foodservice or the ingredient channel." Peter Emsley, vice-president of marketing and sales for Gay Lea Foods, notes, "I could speculate that the increase in butter could be influenced by companies jumping on the reformulation bandwagon to remove trans fats. But we also know that there are other options available as a fat replacement."

### EGGS GET CRACKING

Shell eggs proved to be a remarkable dairy case category. While shoppers bought two per cent more eggs at supermarkets in 2003 they paid nine per cent more for them. Consumers are evidently trading up to the pricier organic and free-range eggs because the CPI for standard Grade A large eggs rose by less than one per cent over the period. Ellen Bevans, a marketing consultant for Burnbrae Farms, which has won Grand Prix awards for its new products Naturegg Omega 3, Naturegg Break Free and Naturegg Omega Pro, attributes the spending surge to the growing popularity of specialty eggs and the willingness of grocers to expand the shelf space for these high margin items. Grade A Brown organic eggs, for example, retail for \$4.89 a dozen in Ontario, more than double the \$2.29 price of the standard Grade A large.

Bernadette Cox says the "Atkins diet has lots of good things to say about eggs and that has certainly helped sales." Cox, manager of public affairs for the Canadian Egg Marketing Agency, adds that the various specialty eggs expand the overall market for eggs as some consumers are attracted by omega-3 fatty acids while others are more concerned

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with avoiding pesticides (organic eggs) or animal welfare (free range).

Consumers' apparent willingness to pay a premium for value-added milk, eggs and dairy products provides a big incentive for processors to invest in product innovations.

DPAC is now working with producers and the federal and provincial governments to eliminate barriers that currently restrict inter-provincial trade and to introduce dairy blend imitation dairy products and other dairy-based products not currently available in Canada.

Whether we look back a year from now to regard the recent upturn as a blip in a flat market or the beginning of a trend will depend on how farmers and regulators respond to this opportunity.

*Doug Burn is a Toronto-based freelance writer and editor and regular contributor to Food in Canada.*

## THE 'NEW' PARMALAT INCLUDES CANADA

As we went to press, it seems more likely that Parmalat Canada will survive the financial meltdown of its parent company Parmalat Finanziaria SpA of Parma, Italy. On March 16, Enrico Bondi, the turnaround specialist appointed by Italy's security regulators as Parmalat's chief executive, presented a restructuring plan that clearly favours the retention rather than sale of Parmalat Canada.

The plan for a 'New' Parmalat clearly anticipates keeping all or most of Parmalat Canada although "a review of the Group's geographic portfolio is in progress with the objective of selecting those countries and businesses that meet these requirements," says Bondi. The plan would eliminate Parmalat's extensive cookie and cracker businesses and 90 of its 120 brands to concentrate on beverages (milk and fruit juices) and related high value added milk products.

Bondi's plan seeks to build on the success of the global brands Parmalat and Santal as well as strong local brands. Parmalat Canada's Astor and Beatrice are two of the 10 brands that Bondi specifically names. Sensational Soy, a drink brand recently launched by Parmalat Canada, is cited as an example of new international brands the company hopes to develop.

It is understandable that the plan would favour Parmalat Canada given its contribution to Finanziaria's top and bottom lines. According to Bay Street analysts, Parmalat Canada is expected to have 2003 sales of \$2.5 billion and an operating profit of \$200 million. That is equal to over 20 per cent of the 5.8 billion Euros in sales Bondi estimates for the parent company and over half of the 200 million Euros in operating earnings. Bondi is proposing a debt-equity swap to Finanziaria's many creditors, a proposition that offers a better but less certain return than a fire sale. Should creditors pull the plug, Parmalat Canada is expected to fetch upwards of \$1.6 billion (it was valued by the company at \$1.2 billion in 2002), enough to reduce the parent company's gross financial debt (now 14.8 billion Euros) by a not insignificant 10 per cent.



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