Confectionery

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I N D U S T R Y P R O F I L E

1990–1991

CONFECTIONERY

FOREWORD

In a rapidly changing global trade environment, the international competitiveness of Canadian industry is the key to growth and prosperity. Promoting improved performance by Canadian firms in the global marketplace is a central element of the mandates of Industry, Science and Technology Canada and International Trade Canada. This Industry Profile is one of a series of papers in which Industry, Science and Technology Canada assesses, in a summary form, the current competitiveness of Canada's industrial sectors, taking into account technological, human resource and other critical factors. Industry, Science and Technology Canada and International Trade Canada assess the most recent changes in access to markets, including the implications of the Canada-U.S. Free Trade Agreement. Industry participants were consulted in the preparation of the profiles.

Ensuring that Canada remains prosperous over the next decade and into the next century is a challenge that affects us all. These profiles are intended to be informative and to serve as a basis for discussion of industrial prospects, strategic directions and the need for new approaches. This 1990–1991 series represents an updating and revision of the series published in 1988–1989. The Government will continue to update the series on a regular basis.

Michael Wilson

Michael H. Wilson
Minister of Industry, Science and Technology
and Minister for International Trade

Structure and Performance

Structure

The confectionery industry comprises manufacturers of all types of sugar confectionery, chocolates and other cocoa-based products, as well as producers of chewing gum. The industry can be divided into two major subsectors — sugar and chocolate confectionery, and chewing gum. The major products in the sugar and chocolate confectionery subsector and the proportion of total industry sales they represent may be broken out as follows: about 34 percent for chocolate bars, about 28 percent for boxed and bulk chocolates, and about 18 percent for hard and soft candies. The chewing gum subsector accounts for about 15 percent of industry shipments, and intermediate and other confectionery products such as bulk chocolate make up 5 percent.

In 1989, the 105 plants in the sugar and chocolate confectionery subsector employed over 6 900 people and manufactured products valued at $840.6 million. The six chewing gum subsector establishments employed nearly 2 200 people and manufactured products worth $270.8 million. Total shipments in 1989 were valued at over $1.1 billion (Figure 1). Exports were valued at close to $165 million in 1989, 66 percent of which went to the United States. In 1989, the balance of trade with the United States was in Canada's favour but, because of imports from other countries, there continued to be an overall trade deficit in confectionery.

In 1989, imports were worth $233 million, representing about 19.8 percent of the Canadian market. Foreign products came mainly from the United States (33 percent) and European countries such as Switzerland, Germany, the United Kingdom, the Netherlands, France and Belgium

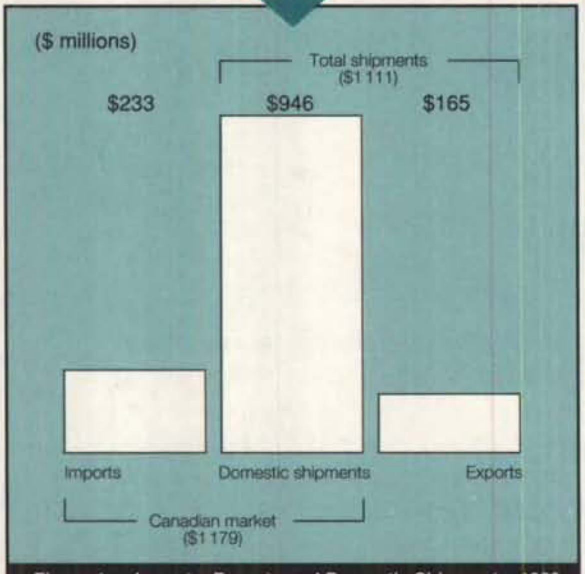

Figure 1 — Imports, Exports and Domestic Shipments, 1989

(about 38 percent). Most of the imported premium-quality boxed chocolates came from Europe. Hard candy imports also originated from these countries and, increasingly, from new suppliers such as Brazil.

Within the chocolate and sugar confectionery subsector, there is a degree of specialization. Most chocolate operations are large and production is dedicated to two major products — boxed chocolates and chocolate bars. Most boxed or packaged chocolates are sold as gifts for birthdays, anniversaries, Christmas, Valentine's Day, Easter, etc. The chocolate bar market tends to be steady year-round but is highly fragmented: a bar that can capture 3 or 4 percent of the market is considered successful. Most of the top 10 brands in the bar market in Canada today have been among the top 10 for close to 60 years.

Most sugar confectionery companies are small or mid-sized and produce a wide variety of products, such as hard candy, gummy bears, licorice, jujubes and toffee, as well as an assortment of hard and soft candies for specialty and novelty markets. Many operations also purchase domestic products or imports for resale under their own labels or to complement their lines. In addition to chewing gum, the chewing gum subsector manufactures other types of confectionery goods or novelty items such as bubble gum with theme cards.

Most confectionery goods are produced in Ontario, which, on average, accounts for about 67 percent of total employment and 65 percent of industry shipments. Quebec follows, with close to 18 percent of employment and 22 percent of shipments.

Production facilities range in size from small one- and two-person seasonal operations to several plants each employing approximately 1 000 people. In 1989, operations with fewer than 20 employees accounted for 70 percent of total establishments, but only about 5 percent of the industry's employment and 3 percent of shipments. On the other hand, about 52 percent of total industry employment is shared among 15 percent of the establishments, which, in turn, contribute 85 percent of total shipments.

One of the largest firms is William Neilson, a domestically owned enterprise. Other Canadian producers include Allan Candy, Dare Foods, Ganong Bros. and Kerr Bros.

Foreign ownership of the confectionery industry is high since multinational enterprises (MNEs) have a major position in the industry. An estimated 60 percent of industry shipments are accounted for by foreign-controlled enterprises located in Canada. Many major Canadian companies are recognizable subsidiaries of foreign-based MNEs: Effem Foods (parent is Mars Inc.), Hershey, Nestlé, Warner-Lambert and Wrigley.

Performance

Total shipments of approximately $1.1 billion in 1989 represented a 20 percent increase over the 1984 value in nominal terms (Figure 2). However, when these figures are adjusted for inflation, which was approximately 23 percent over this period, shipments actually decreased in real terms. In recent years, demand for many domestic confectionery products has decreased slightly. This drop is due in part to a lower proportion of children in the population and to a growing number of calorie- and health-conscious Canadians. Exports have increased slightly from 10.5 percent of shipments in 1984 to 14.9 percent in 1989.

Industry performance is influenced by market forces that affect its ability to achieve high rates of production as well as by competition from imports and the fluctuating cost of some agricultural raw materials.

Although no published data are available on capacity utilization, it is estimated that the industry as a whole operates at only about 75 percent of full production capacity, partly because some specialized equipment is used only for seasonal product lines.

Particularly in the chocolate subsector, the closure of a number of large plants and several mergers during the 1980s have resulted in some consolidation of production facilities and brands. At the same time, a number of small businesses are entering the market. The result is a slight overall increase in the number of firms, with no increase or, in some years, a slight decrease in overall employment over the period.

In 1987, Hershey Canada acquired the confectionery business of Nabisco Brands (makers of Lowney and Moirs

Figure 2 — Total Shipments and Employment

products), which included the Canadian rights for brands such as Oh Henry!, Lifesavers and Planters Peanuts. In the same year, William Neilson acquired the confectionery assets of Canadian Cadbury Schweppes Powell. In 1988, Nestlé Enterprises acquired Rowntree MacIntosh (which in Canada includes the Laura Secord Division). Together with Effem Foods (maker of Mars bars), these four firms dominate the industry. Chiefly a chocolate producer, Hershey also has a significant share of the domestic licorice and hard candy market.

Chewing gum consumption dropped in volume by more than 10 percent between 1982 and 1986, a decline that may be attributed to the decreasing numbers of young people. However, the introduction of new brands featuring non-stick gum for denture wearers or long-lasting flavours and the rapid growth in popularity of sugarless gum have helped to compensate for the decline in mature products.

Another factor affecting performance is the fact that, beginning in 1985, the federal sales tax was extended to most confectionery products but not to competing snack foods. The industry expressed concern that this situation exacerbated declining demand for confectionery products and increased the trend toward alternative snack products such as potato chips, granola and fruit snacks. In the spring of 1987, the federal sales tax was extended to all snack foods; this tax has since been removed from both confectionery products and snack foods and replaced by the goods and services tax (GST). Currently, per capita consumption of confectionery products in Canada is slowly beginning to grow.

Strengths and Weaknesses

Structural Factors

Firms in the confectionery industry compete on the basis of brand names, product advertising and promotion, specialty products, product quality and cost of production.

Because confectionery products are usually discretionary and high-impulse purchases, promotion plays a substantial role in establishing brand-name presence in the various regional markets of Canada. The wide selection of confectionery brands and other snack foods available to consumers encourages considerable promotional expenditures by the industry.

Promotion occurs both within the trade and through the media directly to consumers. The Confectionery Manufacturers Association of Canada estimates that 1989 advertising costs for its members totalled approximately \$57 million, or close to 5 percent of sales. Generally, much more money is expended to promote confectionery brands than other food products. The high cost of national and international advertising is often prohibitive for smaller processors, thereby restricting their entry into some product lines and some markets.

A number of established specialty manufacturers — typically medium-sized and independent firms — have maintained their traditional regional markets through local allegiance or seasonal products rather than strong brand promotion. Ganong Bros., for example, one of the first companies in Canada to sell chocolates in heart-shaped boxes for Valentine's Day, enjoys a 30 percent market share for that specialty product.

To suit domestic taste preferences, Canadian products are sometimes formulated differently from American products. In general, Canadians prefer sweet, creamy chocolate, whereas American consumers prefer less sweet, dark chocolate. This preference provides the industry with additional protection and supports small regional producers who cater to local tastes.

Production costs are sensitive to increases in world sugar, cocoa and nut prices, and the costs of these traded commodities are often volatile. When costs increase significantly, processors have no easy way to pass them along to consumers while retaining their traditional share of the confectionery market.

Confectionery can lose its relative share of the snack food business when product prices rise. During periods of volatile ingredient costs, there is increased intra-industry competition. Because manufacturers are reluctant to raise their prices, they often attempt to reformat products to compensate. However, this practice disrupts the normal production process and depresses profits. In addition, Canadian multinationals, which make some products for export to their U.S. parent companies, are less competitive when sugar prices rise.

Packaging materials represent a significant input cost, estimated at over 26 percent of the cost of raw materials. The primary product ingredients used and their approximate percentage cost of raw materials are cocoa products (35 percent), sugar (12 percent), dairy products (7 percent) and nuts (5 percent).

Canadian producers generally enjoy an advantage over American producers when competing in the United States market: the United States maintains a high domestic price for sugar, while Canadian processors derive a significant benefit from their ability to purchase sugar at generally lower world prices. On the other hand, the playing field is levelled for U.S. producers on the world market under a re-export program whereby they can buy sugar at world prices, provided that the resulting product is destined for the export market.

Canadian dairy prices, which are considerably higher than those of other developed countries, place milk chocolate producers at a disadvantage in the domestic market relative to imports. Competitive dairy prices can, however, be negotiated with the Canadian Dairy Commission for confectionery products destined for external trade.

Trade-Related Factors

The Canadian tariff rates on products imported from countries having Most Favoured Nation (MFN) status are 12.5 percent ad valorem for confectionery containing chocolate, and they range from 15.5 to 16.7 percent ad valorem for sugar candy and other confectionery items. The MFN tariffs in Canada's major export market, the United States, range from 5 to 7 percent ad valorem on chocolate confectionery as well as for all other confectionery items. The Canada-U.S. Free Trade Agreement (FTA), which was implemented on 1 January 1989, is phasing out tariffs on all confectionery goods by 1 January 1998 in 10 annual, equal steps. In the European Community (EC), tariffs on imports range from 12 to 27 percent ad valorem, but there is also an additional levy on all sugar-containing products, depending on the amount of sugar found in the product. The tariff plus the levy translates into tariff protection ranging from 30 to 60 percent ad valorem on most confectionery products.

Because of a waiver under the General Agreement on Tariffs and Trade (GATT), the United States currently imposes quotas on the import of some sugar-containing products, but confectionery goods have not been included. In the past, the restrictions have been applied only to selected products containing sugar on the grounds that such products undermine the U.S. sugar policy.

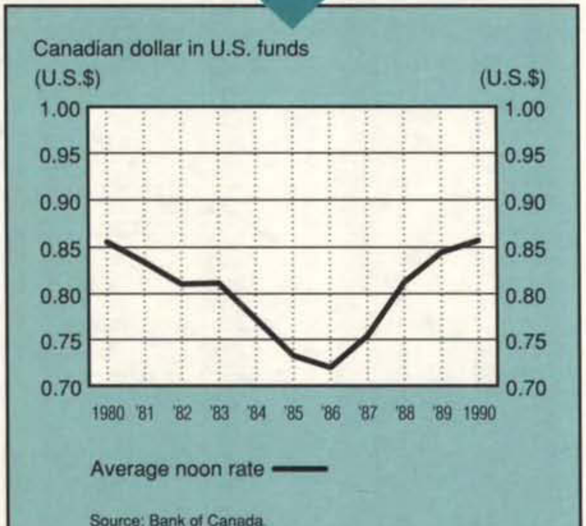

Figure 3 — Canadian–U.S. Exchange Rates

The industry has expressed concern about the relatively higher value of the Canadian dollar in recent periods vis-à-vis the American dollar (Figure 3). On the other hand, under certain economic conditions, it is widely recognized that a significantly lower value is likely to be inflationary. The resulting higher domestic costs and prices can erode, over time, the short-term competitive gains of such a lower-valued dollar.

Technological Factors

The large and mid-sized firms in the Canadian confectionery industry are generally capital-intensive, technologically modern and efficient. Entry to the industry, however, can be gained by firms with low levels of technical sophistication. Smaller firms often use older equipment and run labour-intensive operations, since they do not have sufficient sales volume to warrant investment in some of the newer high-speed, high-capacity machinery.

New developments in confectionery technology are few compared with other industries and are usually developed by machinery manufacturers. Most firms are well informed of new international process developments, the majority of which are available off the shelf. Proprietary process improvements, new product formulations and ingredient improvements occur regularly, especially within larger MNEs. These advancements are often shared with their Canadian subsidiaries.

Evolving Environment

In recent years, product lines and trade names have been consolidated through mergers and acquisitions. This has led to greater concentration of market shares, resulting in the increased plant efficiencies necessary to compete internationally. The same phenomenon is taking place in the United States. However, brand-name acquisitions made by American parent firms do not necessarily correspond with those made by their Canadian subsidiaries. For example, Cadbury Schweppes (U.S.) was acquired by Hershey (U.S.), while in Canada the Cadbury Schweppes Powell lines were acquired by William Neilson. Nestlé (U.S.) owns the Oh Henry! brand, but Hershey Canada acquired the Canadian rights to Oh Henry! when it purchased the Nabisco confectionery businesses. Instead of building strong international company allegiances or trade goals, acquiring brand labels is a way for MNEs to prevent the erosion of their domestic market share.

Demand for many industry products has suffered because of changing demographic influences such as slow population growth and growing numbers of calorie- and health-conscious consumers. Products developed to meet consumer concerns about dental caries and high-calorie foods include a variety of sugarless gum products, which are enjoying a growing market share. Sugarless gums are now estimated to represent about 55 percent of overall sales in Canada, compared with 20 percent in 1984. As the cost of artificial sweeteners such as Aspartame continues to decrease, and as regulations governing their use are eased, more "light" or low-calorie confectionery products are expected to be developed for this growing market.

In an effort to increase consumption of confectionery products, the Confectionery Manufacturers Association of Canada is undertaking a public information campaign to combat some of the negative perceptions associated with eating confectionery products. This campaign includes educating health care professionals and distributing a brochure display system to be set up in dentists' offices across the country. The brochure refers to recent research in dentistry and nutrition indicating that candy and confectionery are no more a threat to dental health than a broad range of everyday foods, such as fruits, vegetables, pastas or bread, since any food that contains sugars or starches is implicated in the development of tooth decay.

The growth of retail gourmet candy shops indicates an emerging specialty market that recognizes the consumer's willingness to buy quality confectionery products at premium prices. The present volume of commerce is small but increasing. Most retail shops base their merchandise on imported goods, but domestic producers are starting to supply the gourmet specialty market with quality chocolate products. The industry continues to face stiff competition, though, with high-quality products coming from Europe. These imports of premium chocolates, as well as hard candies, have been taking an increasing share of the total Canadian market over the past decade.

The United States market offers potential for specialty products, particularly in large border markets. While a tariff-free environment and lower sugar costs should encourage additional exports to the American market, Canadian firms still need to reduce costs and become more efficient. Early in 1991, William Neilson, encouraged by results of a taste-test survey and the prospect of freer trade under the FTA, sent its first shipment of Crispy Crunch, Canada's top-selling chocolate bar, south of the border. The bar is being promoted in the U.S. as "Canada's Favourite Bar." Plans are also under way for the company to begin marketing its Mr. Big bar in the United States. It already sells this bar in the Taiwan market under the name Bang Bang. Ganong Bros. is one of the companies that are turning their marketing efforts to Pacific Rim countries. The company is involved in a joint-venture project with a Thailand-based trading and manufacturing company, and it is enjoying a growing volume of exports to Japan, where there is a strong demand for Western-type consumer products.

The industry has expressed concern about the equitable enforcement of Canadian labelling standards on products that fall under the *Consumer Packaging and Labelling Act* and the *Food and Drugs Act*, which are the shared responsibility of Consumer and Corporate Affairs Canada (CCAC) and Health and Welfare Canada. Since October 1989, increased efforts have been undertaken to ensure compliance with Canadian standards covering bilingual labelling and metric declaration, ingredient declarations, nutritional claims, and the use of ingredients permitted in Canada. In response, CCAC and Revenue Canada Customs and Excise are jointly conducting a program that focuses on compliance surveillance and inspection of imported food at selected border points. This initiative has intercepted significant volumes of imported products and has ensured that labelling violations were corrected. The Confectionery Manufacturers Association of Canada, along with other food industry associations, has assisted in this initiative by identifying instances of non-compliance. The industry continues, though, to view the problem as a serious threat to its overall competitiveness.

Packaging is the major environmental issue facing the industry in the 1990s. The confectionery industry is preparing to meet the goals of the National Packaging Protocol, sponsored by the Canadian Council of Ministers of the Environment, which calls for an overall reduction of 50 percent of packaging waste sent for disposal by the year 2000, relative to the base year of 1988. Processors are seeking ways to apply the 3R (reduce, reuse, recycle) strategy to their operations and products. Many individual firms are conducting environmental audits of their manufacturing processes and are developing environmental profiles of their packaging materials in order to identify means of reducing packaging waste without compromising legislated health and safety requirements or consumer demand for convenience and utility. As well, many firms are using shipping cases and cartons made of recycled board, which are in turn recycled. Despite these efforts, waste packaging from confectionery products is extremely visible as litter, and therefore contributes to the perception that confectionery is over-packaged. This perception places considerable pressure on the industry to reduce the amount of packaging it uses.

Competitiveness Assessment

A series of rationalizations within the industry has resulted in more efficient operations, and most large and mid-sized firms are now using modern equipment. However, the industry will need to enhance formulations, particularly in its premium chocolate products, to compete with growing imports in this area. The industry must also continue to increase its export sales to compensate for a domestic market that is exhibiting very little real growth.

The Canadian industry is in the process of adapting to a more open trading environment, although the FTA should have a relatively limited impact on the industry. Some Canadian confectionery manufacturers may face scale disadvantages compared with American firms but, at the same time, the Canadian industry enjoys a cost advantage in sugar. Taste differences, specialized products and differing brands or brand ownership may also help separate the two markets.

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PRINCIPAL STATISTICS[a]

	1983	1984	1985	1986	1987	1988	1989
Establishments	93	94	99	113	97	110	111
Employment	9 096	9 014	9 265	8 908	8 802	8 873	9 087
Shipments ($ millions)	866	928	990	986	1 027	1 024	1 111
Investment[b] ($ millions)	40.7	30.0	29.4	37.5	74.9	51.0	N/A

[a]For establishments, employment and shipments, see *Food Industries*, Statistics Canada Catalogue No. 32-250, annual (SIC 1082, chewing gum industry, and SIC 1083, sugar and chocolate confectionery industry).

[b]See *Capital and Repair Expenditures, Manufacturing Subindustries, Intentions*, Statistics Canada Catalogue No. 61-214, annual.

N/A: not available

TRADE STATISTICS

	1983	1984	1985	1986	1987	1988[a]	1989[a]
Exports[b] ($ millions)	53	97	91	129	137	122	165
Domestic shipments ($ millions)	813	831	899	857	890	902	946
Imports[c] ($ millions)	143	196	206	222	239	229	233
Canadian market ($ millions)	956	1 027	1 105	1 079	1 129	1 131	1 179
Exports (% of shipments)	6.1	10.5	9.2	13.1	13.3	11.9	14.9
Imports (% of Canadian market)	15.0	19.1	18.6	20.6	21.2	20.2	19.8

[a]It is important to note that data for 1988 and after are based on the Harmonized Commodity Description and Coding System (HS). Prior to 1988, the shipments, exports and imports data were classified using the Industrial Commodity Classification (ICC), the Export Commodity Classification (XCC) and the Canadian International Trade Classification (CITC), respectively. Although the data are shown as a continuous historical series, users are reminded that HS and previous classifications are not fully compatible. Therefore, changes in the levels for 1988 and after reflect not only changes in shipment, export and import trends, but also changes in the classification systems. It is impossible to assess with any degree of precision the respective contribution of each of these two factors to the total reported changes in these levels.

[b]See *Exports by Commodity*, Statistics Canada Catalogue No. 65-004, monthly.

[c]See *Imports by Commodity*, Statistics Canada Catalogue No. 65-007, monthly.

REGIONAL DISTRIBUTION[a] (average over the period 1986 to 1988)

	Atlantic	Quebec	Ontario	West
Establishments (% of total)	6	31	41	22
Employment (% of total)	7	18	67	8
Shipments (% of total)	10	22	65	3

[a]ISTC estimates.

MAJOR FIRMS

Name	Country of ownership	Location of major plants
Allan Candy Ltd.	Canada	Hamilton, Ontario
Dare Foods (Candy Division) Limited	Canada	Kitchener, Ontario Hamilton, Ontario Milton, Ontario
Effem Foods Ltd.	United States	Surrey, British Columbia Bolton, Ontario
Ganong Bros. Ltd.	Canada	St. Stephen, New Brunswick
Hershey Canada Inc.	United States	Smiths Falls, Ontario
Kerr Bros. Limited	Canada	Toronto, Ontario
William Neilson Ltd.	Canada	Toronto, Ontario
Nestlé Enterprises Limited (Confectionery Division)	Switzerland	Don Mills, Ontario
Warner-Lambert Canada Inc.	United States	Scarborough, Ontario
Wrigley Canada Inc.	United States	Don Mills, Ontario

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