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SECTOR COMPETITIVENESS FRAMEWORKS

HOUSEHOLD FURNITURE

PART 1 – OVERVIEW AND PROSPECTS

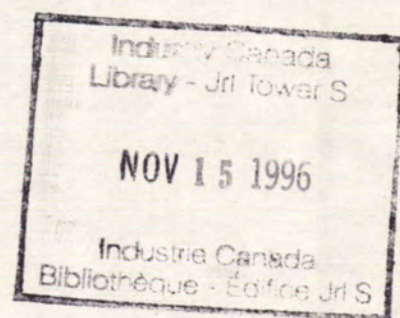
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Canada

HOUSEHOLD FURNITURE

PART 1 — OVERVIEW AND PROSPECTS



PREPARED BY:
**FASHION, LEISURE AND
HOUSEHOLD PRODUCTS
BRANCH**

This *Overview and Prospects* is the first of two companion documents on Household Furniture in the **Sector Competitiveness Frameworks** series, which is being produced by Industry Canada in partnership with Canada's key stakeholders in the industry. *Part 2 — Framework for Action* will be prepared in coming months, based on consultations with major industry stakeholders, following study and review of the *Overview and Prospects*.

The **Sector Competitiveness Frameworks** series will focus on the opportunities, both domestic and international, as well as on the challenges facing each sector. The objective is to seek ways in which government and private industry together can strengthen Canada's competitiveness and, in doing so, generate jobs and growth.

In all, some 29 industrial sectors will be analyzed. *Part 1 — Overview and Prospects* will be available for distribution in printed as well as electronic forms during coming months for the following industries:

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FOREWORD

The new Canadian marketplace is expanding from national to global horizons and its economic base is shifting increasingly from resources to knowledge. These trends are causing Canadian industries to readjust their business approaches, and government must respond with new tools to help them adapt and innovate. Industry Canada is moving forward with strategic information products and services in support of this industry reorientation. The goal is to aid the private sector in what it is best qualified to do — create jobs and growth.

Sector Competitiveness Frameworks are a series of studies published by Industry Canada to provide more focussed, timely and relevant expertise about businesses and industries. They identify sectors or subsectors having potential for increased exports and other opportunities leading to jobs and growth. In 1996–97, they will cover 29 of Canada's key manufacturing and service sectors.

While they deal with “nuts and bolts” issues affecting individual sectors, the Sector Competitiveness Frameworks also provide comprehensive analyses of policy issues cutting across all sectors. These issues include investment and financing, trade and export strategies, technological innovation and adaptation, human resources, the environment and sustainable development. A thorough understanding of how to capitalize on these issues is essential for a dynamic, job-creating economy.

Both government and the private sector must develop and perfect the ability to address competitive challenges and respond to opportunities. The Sector Competitiveness Frameworks illustrate how government and industry can commit to mutually beneficial goals and actions.

The Sector Competitiveness Frameworks are being published sequentially in two parts. An initial *Overview and Prospects* document profiles each sector in turn, examining trends and prospects. The follow-up *Framework for Action* draws upon consultations and input arising from industry–government collaboration, and identifies immediate to medium-term steps that both can take to improve sectoral competitiveness.



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ousehold furniture making has been a part of Canada's industrial base since the inception of the country.

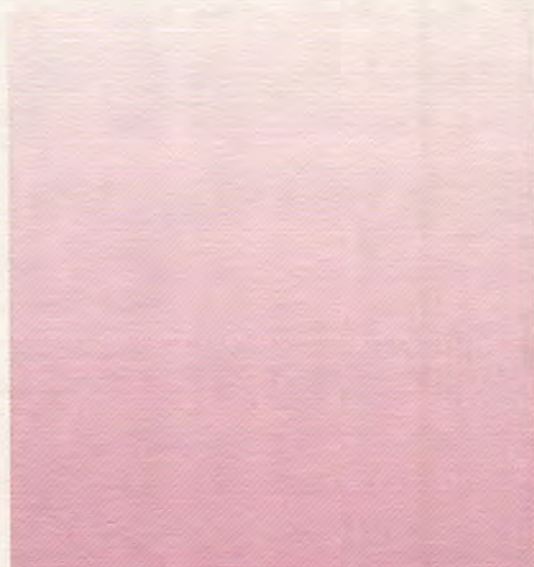
In 1994, the industry comprised

578 plants, employing 19 536 people, with shipments valued at \$1.72 billion. Some 62 percent of shipments consisted of wooden furniture, 29 percent upholstered furniture and 9 percent metal and plastic furniture. In 1995, industry shipments rose to an estimated \$1.83 billion.

The industry serves the consumer market, and sells products through retail outlets. The Canadian market in 1995 was estimated at \$1.79 billion, a slight decline from \$1.8 billion in 1994. The market is heterogeneous, with a wide variety of consumer preferences.

While the industry accounts for only 1.2 percent of manufacturing employment in Canada and 0.5 percent of manufacturing shipments, it is the third largest customer of the Canadian textiles industry and consumes about a third of all hardwood lumber production in Canada. With a 2-percent share of the world market for household furniture, Canada is a relatively small player on the world scene. However, it is located next to the world's largest market, the United States, which offers unique opportunities for exporters with competitive products.

This highly fragmented industry is primarily composed of a few large firms (the largest manufacturer reported sales of \$334 million in 1994) and many small ones. Barriers to market entry



into the industry are still low. It is predominantly Canadian-owned, with a strong family ownership tradition. The industry is represented in both small and large communities across the country.

1.1 Trend Indicators

In response to generally favourable market conditions, the industry achieved a solid record of expansion during the 1983–87 period. The industry then underwent extensive restructuring in the late 1980s and early 1990s coinciding with a recession and following the growing import pressure from the United States as a result of the implementation of the Canada–U.S. Free Trade Agreement (FTA). Historically, the industry had developed behind high tariff walls. The restructuring has resulted in a significant decline in the number of manufacturers, a more rationalized and specialized structure of production and a reorientation of marketing effort toward the U.S. to compensate for declining domestic demand.

Innovation and Investment

The household furniture industry worldwide generally relies on suppliers of materials, machinery and equipment to conduct research and development (R&D) activities. Most of the R&D is done outside Canada.

Relative to the manufacturing sector, new investments by the Canadian household furniture industry are modest. More important, the Canadian industry invests less capital per worker than its U.S. counterpart. Poor financial performance over the past few years has reduced the Canadian industry's access to capital and its ability to invest in much needed modern production

technologies. Consistent with the lower levels of investments, productivity in the Canadian industry was 23.1 percent lower than U.S. industry productivity in 1992. The larger scale of U.S. plants is also a factor responsible for the difference in productivity.

Investments during the past few years have focussed on the acquisition of computer-aided design (CAD) equipment and computer numeric controlled (CNC) machines. About 40 percent of Canadian firms have adopted CAD equipment and CNC machines. These technologies have led to improvements in plant productivity and in the quality and appearance of Canadian furniture. In addition, the federal and several provincial governments have provided important financial support for many years to encourage firms to develop innovative designs. However, while a growing number of Canadian manufacturers are known for their strong design capabilities, the industry still largely imitates U.S. and European designs.

Human Resources

The industry is labour intensive. It employs primarily unskilled and semi-skilled workers, especially immigrants. Wage rates in the industry are below the average for the manufacturing sector in Canada. However, the Canadian industry has slightly higher wage costs (excluding fringe benefits) than its U.S. counterpart. The wage gap is partially offset by the lower salary costs of non-production employees.

Labour supply has not been a critical problem for the Canadian industry, although specialized skill shortages continue to exist. In addition, the introduction of more computerized machinery and equipment in the past few years has led to a requirement for better-educated workers.

Due in large measure to the entrepreneurial nature of most firms in the Canadian industry, there is a general lack of professional management. In particular, the industry lacks marketing management strengths. The orientation of many owners in this industry is essentially toward the production aspect of the business. The U.S. industry is generally regarded to put more emphasis on marketing than its Canadian counterpart.

Industry Canada has been an important partner in recent efforts by Human Resources Development Canada to identify skill gaps and to support the development of new education and training programs for the industry's workers and managers. Over the next few years, the industry will have to invest substantially in its human capital to realize the full benefit that could be realized from the adoption of new production and information technologies.

Trade

In 1995, the Canadian household furniture industry recorded its first trade surplus, \$35 million. This is quite an achievement when compared with a deficit peaking at \$370 million in 1992. Exports tripled between 1988 and 1995 to reach \$728 million, or 39.8 percent of industry shipments. However, the bulk of Canadian exports still originates from a small number of firms, mostly large ones. The industry has been particularly successful in exporting wooden furniture. The most successful exporters generally focus on design and quality rather than on price. Canada has traditionally been dependent on the U.S. as its primary export market. That country absorbed 95.7 percent of Canadian exports in 1995. Canada's share of the U.S. market is about 1.5 percent, leaving significant room for expansion.

The Department of Foreign Affairs and International Trade, in partnership with Industry Canada, has been active for many years in developing a stronger sense of export awareness among small and medium-sized enterprises and in helping firms to identify and exploit export market opportunities.

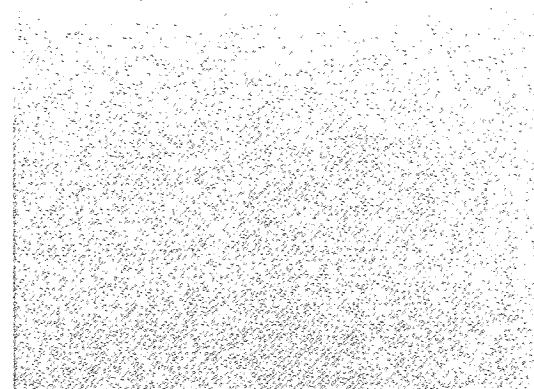
Between 1988 and 1995, imports into Canada doubled to reach \$693 million, accounting for 38.7 percent of the domestic market. The U.S. is Canada's largest source of imported furniture, supplying 62.2 percent of all imports in 1995, followed by low-wage countries (primarily Taiwan and China), with a share of 24.3 percent. The loss of market share to imports over the past few years was most severe in upholstered furniture.

Sustainable Development

Although the processes used in household furniture manufacturing do not give rise to serious pollution problems, an increasing number of manufacturers are learning that it makes good business sense to reduce the environmental impact of their products. For example, Canadian firms have reduced the levels of volatile organic compound (VOC) emissions.

Other Factors

While it is a major user of Canadian input materials, the industry must import an important portion of its requirements. Therefore, because Canada levies higher tariffs on furniture input materials imported from nations with which it has established Most Favoured Nation (MFN) status than the United States does, the Canadian furniture industry faces cost disadvantages when these materials are sourced outside North America. The reduction of tariffs on input materials negotiated during the



Uruguay Round of multilateral trade negotiations under the General Agreement on Tariffs and Trade (GATT) and implemented in 1995 under the World Trade Organization (WTO), which replaced the GATT, will put Canadian firms on a more level playing field relative to U.S. manufacturers.

Given its fragmentation, a strong national association could play an important role in this industry. However, regional rivalries have prevented the national trade association (i.e. the Canadian Council of Furniture Manufacturers) from acting as an effective information clearing house.

1.2 Outlook

Short-term domestic demand in this sector depends largely on consumer disposable income and hence on the vagaries of the economic cycle. Medium-term domestic demand depends primarily on household formation and housing starts. Over the next decade, the Canadian market is forecast to expand at an average annual growth rate of about 1 percent in real terms (after discounting inflation), compared with a projected rate of 1.5 percent for total consumer expenditures. However, several product niches will offer above-average growth, including furniture that meets the physical needs of the elderly and furniture geared toward home entertainment centres. Key consumer niche markets include high income earners and new immigrants. Most of Canada's population growth will be through immigration. Immigrant tastes in furniture are expected to emulate those in North America. One avenue the industry is examining to boost domestic demand is to shift consumer perception of furniture from a "commodity" to a "fashion" item, thus speeding up the replacement cycle for new furniture.

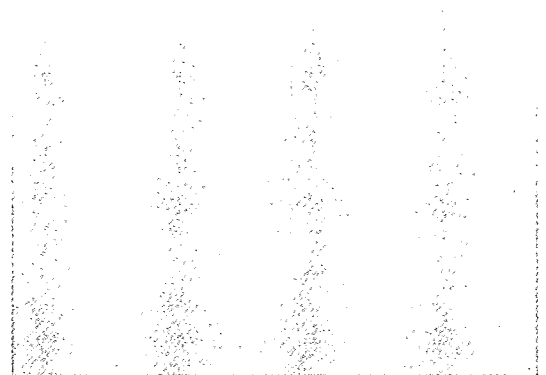
To overcome the problems associated with the small size of the Canadian market and the expected relative weakness in domestic consumer demand over the medium term suggests increased efforts in the export field. Good opportunities for Canadian exporters are expected in export markets, particularly in the U.S., where demand is projected to grow at an annual rate of 2–3 percent. In addition, the tariff reductions implemented under the North American Free Trade Agreement (NAFTA) will give Canadian exporters improved access to Mexico, while those implemented under the WTO will create new opportunities in western Europe and the Asia Pacific areas. However, trade liberalization will also lead to increasing trade competition both at home and abroad.

The industry will also have to face an increasingly concentrated and demanding retailing sector. This will force manufacturers to re-examine their marketing strategies as well as the nature and extent of their intra-linkages with retailers.

1.3 The Bottom Line

The Canadian household furniture industry has had to make significant adjustments in response to the FTA. The industry has had to transform itself at a forced pace to face higher import pressures, and also to take advantage of new export opportunities in the world's largest household furniture market, the United States. However, the industry recognizes that there is room for further improvement.

The industry is at a crossroads in its development. The positive environment created by the competitive advantages of the low exchange rate for the Canadian dollar relative to U.S. currency



provides a window of opportunity to the industry to attack its weaknesses. These include overcoming fragmentation, controlling costs, improving productivity, updating equipment and technology, improving worker and management skills, and improving design and marketing. These and other issues will be addressed properly and jointly with the industry and other stakeholders in the upcoming *Part 2 — Framework for Action* document of the Sector Competitiveness Frameworks series.

2 KEY POINTS ABOUT THIS INDUSTRY

Canada possesses a long-standing and well-established household furniture industry that transforms relatively low-value-added materials, such as lumber and particleboard, into high-value-added, finished consumer goods. This major industry group is defined by Statistics Canada under Standard Industrial Classification (SIC) 261, which comprises establishments primarily engaged in manufacturing household furniture of all kinds and all materials, including outdoor furniture but excluding mattresses, bed springs, reupholstering and repairs. Canada's primary strength in this sector is wooden furniture of innovative design and good quality.

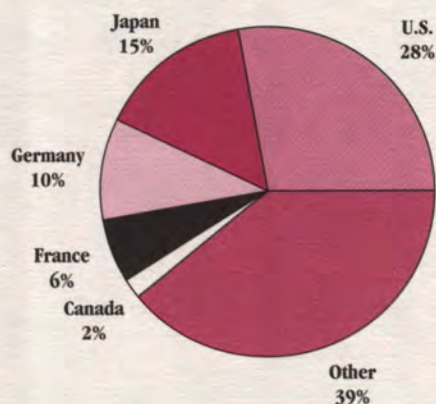
2.1 Global Context

With an estimated value of about \$95 billion in 1993, the global market for household furniture shows a wide range of consumer preferences in terms of style, design, uniqueness, quality and price. Canada accounts for only 2 percent of the global market, but is located next to the world's biggest market, the United States, which makes up 28 percent of the world market. The U.S. is also the home base of most of the world's biggest manufacturers. Other major world markets are Japan at 15 percent and Germany at 10 percent (Figure 1).

Canada's furniture industry makes high-value-added, high-quality products

Canada claims 2% of global market, dominated by U.S. at 28%

Figure 1. World Market for Household Furniture, 1993



Source: Industry Canada estimates.

World trade opportunities growing for unassembled furniture

While 1993 world trade in household furniture accounted for only about 0.9 percent of merchandise trade, it has been growing at a slightly faster rate than merchandise trade overall in recent years, primarily due to increased shipments of unassembled furniture. Italy and Germany are the world's largest exporters, but several low-wage Asian countries (particularly Taiwan and China) are becoming more active on the international scene.

2.2 North American Context

95% of Canada's furniture exports go to U.S.

Canada in 1995 sold 95.7 percent of its household furniture exports to the United States, making up 14 percent of the U.S. import market. This was below the share of Taiwan at 18.1 percent but above that of all other countries, including Italy with a share of 12.5 percent and Mexico at 6.6 percent.

FTA led to rapid industry adjustment

Being located next to the U.S. offers Canadian furniture manufacturers unique opportunities and challenges. A rapid and pronounced adjustment in this industry took place following the removal of tariff protection on household furniture after implementation of the Canada-U.S. Free Trade Agreement (FTA) in 1989 and a business recession in 1990-91. The number of firms declined by half, while employment dropped by one third. A large cross-section of the remaining firms introduced competitiveness improvement measures, resulting in a more rationalized and specialized structure of production and a dramatic increase in exports to the United States.

Competitiveness depends on positioning relative to the U.S.

The North American Free Trade Agreement (NAFTA) among Canada, the United States and Mexico has not exerted strong pressures for adjustment in the Canadian industry to date. In the wake of freer trade, Mexico presents modest market opportunities for Canadian household furniture exports.

However, Canadian furniture producers can expect increased import pressure from Mexican products. In this freer trade environment, the continued competitiveness of the Canadian industry hinges primarily on how well it is positioned relative to its U.S. counterpart.

The industry recognizes that it must continuously improve, even in the areas where performance is considered superior. The main current factors affecting Canadian competitiveness vis-à-vis its major competitor, the United States, include higher but declining tariffs levied on input materials imported from countries having Most Favoured Nation (MFN) status with Canada, higher labour costs, lower capital investment and lower productivity. There is also a need for stronger design capabilities and marketing skills to help assure continuing presence in the U.S. market and to assist in expanding exports to other foreign markets. In addition, a strong national association could play an important role in this highly fragmented industry.

2.3 Canadian Industry Snapshot

Household furniture has been part of Canada's industrial base from early settlement. Most early plants were small, family-owned and located in the hardwood-producing regions of Ontario and Quebec far from major urban centres. The first industrial plant was established in Kitchener in 1830.

Canada's 578 plants in 1994 employed 19 536 people, and generated \$1.72 billion worth of shipments. The average plant employed 34 people and generated shipments valued at \$3 million, compared with 52 employees and \$11 million in shipments for the average factory in the overall Canadian

Challenges to the industry:

- costs
- equipment age
- productivity
- design
- marketing

"Our European ancestors were thrown back on the simplest and most fundamental of human resources. Their furniture was a reminder and proof of identity and tradition."

**— William Kilbourn,
The Heritage of Upper
Canadian Furniture**

**Canada exports 40% of
industry production . . .**

... and the industry
supplies 61% of the
Canadian market

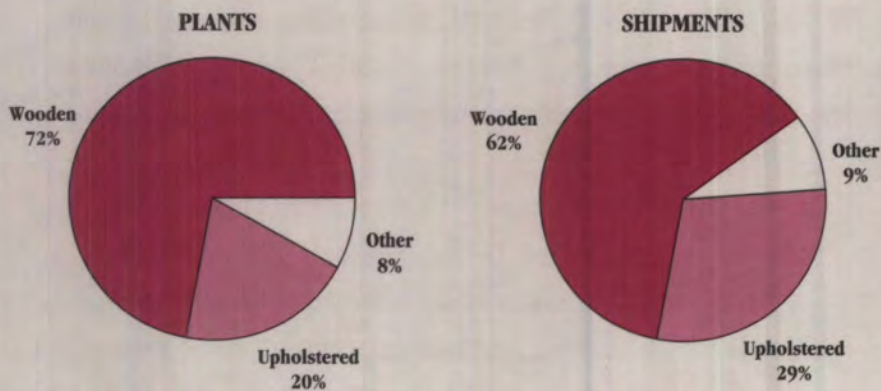
... accounts for 0.5% of
manufacturing shipments,
contributes 0.6% to GDP

manufacturing sector. The wooden furniture subsector accounted for 72 percent of all furniture plants and 62 percent of industry shipments (Figure 2). Statistics Canada estimates shipments in 1995 at \$1.83 billion, of which 39.8 percent were exports. The Canadian market was valued at \$1.8 billion in 1994, but declined to an estimated \$1.79 billion in 1995, of which 61.3 percent was supplied by domestic manufacturers.

In 1994, the industry contributed 1.8 percent of all Canadian manufacturing sites, 1.2 percent of manufacturing employment, 0.5 percent of manufacturing shipments, 0.6 percent of manufacturing value-added and 0.6 percent of manufacturing gross domestic product (GDP).

By comparison, the U.S. industry has approximately seven times as many plants, 12 times the employees and 15 times the shipments of the Canadian industry. The average U.S. plant is twice the size of its Canadian counterpart (Annex A provides comparative statistics).

Figure 2. Contribution of Subsectors to the Canadian Household Furniture Industry, 1994



Source: Statistics Canada, Catalogue No. 35-251.

The industry is the third largest customer of Canadian textiles, and consumes about a third of all Canadian hardwood lumber production. The costs of materials and supplies represented 49.2 percent of industry shipments in 1994, almost 10 percentage points below the average for all manufacturing industries in Canada. Materials and supplies accounted for an estimated 49 percent of the U.S. household furniture industry's shipments (see Annex B for more detail on intermediate inputs).

Furniture is third largest consumer of Canadian textiles, uses a third of hardwood lumber

Personal expenditures on household furniture represent about 1 percent of all consumer spending on goods and services in Canada.

The strong family ownership tradition in this industry has kept ownership private and has deterred consolidation. Fewer than 1 percent of firms are foreign controlled.

Family firms keep furniture 99+% Canadian

The vast majority of firms are single-plant operations. The industry has a large number of small entrepreneurial firms and a small number of large firms. Market barriers to entry are still relatively low, but are becoming higher as the industry adopts more expensive production technologies. Small firms are usually short of capital, technology and management skills, and usually serve a local/regional market. Larger firms usually keep abreast of technological changes, have professional management and a strategic perspective, and account for the bulk of Canadian exports.

The two largest Canadian firms in terms of revenue, Dorel Industries Inc. (\$334 million in 1994) and Palliser Furniture Ltd. (an estimated \$240 million in 1994), have become international producers. Palliser generated roughly 85 percent of revenue from Canadian-based plants and 15 percent from U.S.-based plants. Dorel shows the opposite pattern: an 83:17 split in favour of foreign production, with plants in Europe, Asia and the U.S.

The two largest Canadian firms are international

**Canada's larger firms seem
small relative to U.S. firms**

Three of the top 10 firms are publicly owned: Dorel, Shermag Inc. and Bestar Inc. La-Z-Boy Canada Ltd., the largest foreign-owned company, generates the fourth highest revenue. Firms considered large in Canada are small relative to their international competitors; the largest U.S. manufacturer produces as much as the entire Canadian industry.

A few Canadian household furniture manufacturers are vertically integrated upstream. The U.S. industry is considered to be more integrated.

**Since the FTA, there
are fewer firms, but they
compete more vigorously**

Prior to implementation of the FTA in 1989, the industry was highly segmented, peaking at 1157 establishments in 1988. The top 10 plants accounted for a relatively low 16.8 percent of industry shipments and the top 100 for only 61.9 percent. By 1994, increased import pressure following the elimination of tariffs under the FTA, as well as recessionary pressures during 1990-91, had led the number of establishments to fall by 50 percent to 578. Less efficient or financially weak plants closed as a result of actual and prospective market share losses. By 1994, the top ten establishments accounted for 21.7 percent of industry shipments, while the top 100 had consolidated their share at 73.9 percent.

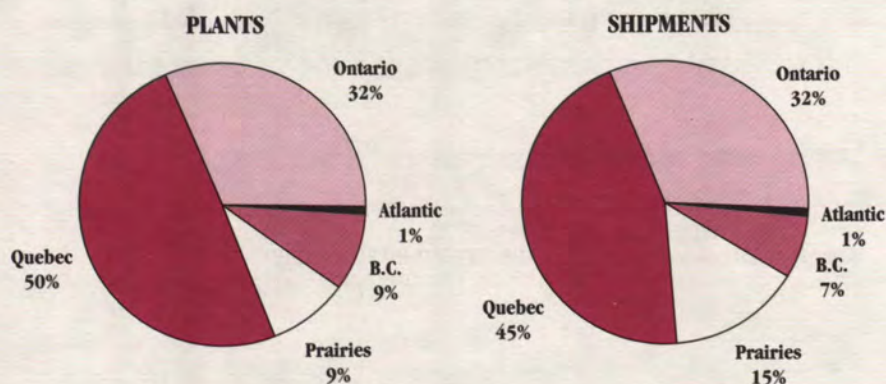
**Canadian firms are
too small to set prices,
control entry to industry**

Because of the continuing large number of small domestic firms, the industry has a high degree of competition. Canadian firms do not have market power to set prices or control entry into the industry. High import penetration, particularly in the upholstered furniture subsector, further increases competition.

Regionally, Quebec accounted for 45 percent of 1993 shipments (the latest year for which such data are available), Ontario 32 percent, the Prairies 15 percent, British Columbia 7 percent and the Atlantic region 1 percent (Figure 3). Prairie plants were about twice as large, on average, as those in the rest of the country; shipments averaged \$4.5 million per Prairie plant compared with \$2.4 million in shipments per plant in the other regions. While the industry provides needed employment in smaller communities, it also operates in highly populated centres.

**Quebec ships 45%
of Canada's furniture
production, Ontario 32%**

Figure 3. Regional Distribution of Canadian Household Furniture Industry Plants and Shipments, 1993



Source: Statistics Canada, Catalogue No. 31-203.

Some product specialization exists regionally, wooden furniture production is largely concentrated in Quebec, while upholstered products are largely made in Ontario.

The national trade association is the Canadian Council of Furniture Manufacturers (CCFM), a non-profit umbrella organization based in Winnipeg. The CCFM represents three regional associations: Furniture West, the Ontario Furniture Manufacturers Association and L'Association des fabricants de meubles du Québec. Their membership accounts for about 50 percent of total Canadian household furniture shipments.

**Regional trade associations
need to find common ground**

Furniture trade show organization is a major activity of the regional associations, and these have become an important venue for sales to retailers. Associations use show revenue to finance many of the other services they provide to their members. At times, show organization has become a major source of friction between regional associations, and has tended to hamper their ability to develop common positions and resolve common problems.

Employment and Labour Market

The industry employed 19 536 people in 1994, a 34.4 percent decline from the 1987 peak. The decline in employment appears to have bottomed out.

**Furniture is
labour intensive**

The industry is labour intensive. Wage costs represented 21.1 percent of industry shipment value in 1994, almost 10 percentage points above the average for all manufacturing industries in Canada, and an estimated five points above the U.S. household furniture industry average.

**The industry offers mostly
low-wage, low-skill jobs**

Household furniture is considered a low-wage industry, reflecting the relatively low skill requirements of most of its occupations; average hourly wages were \$10.50 in 1994, about 67 percent of the average manufacturing wage. Nevertheless, larger household furniture companies tend to pay higher-than-average wages for the industry to attract the best workers.

About one quarter of the Canadian industry labour force is unionized. The primary union is the United Steel Workers of America. The larger companies tend to be unionized. Unionization in the U.S. is considered to be lower than in Canada.

Many of the tasks involved in making household furniture are highly repetitious. As a consequence, much of the labour force need not be highly skilled; in Canada, 40 percent of the industry's labour force do not have a secondary school diploma. However, as a result of the introduction of more computerized processes, there has been growing demand for more highly literate workers. The majority of trade skills are acquired informally, on the job.

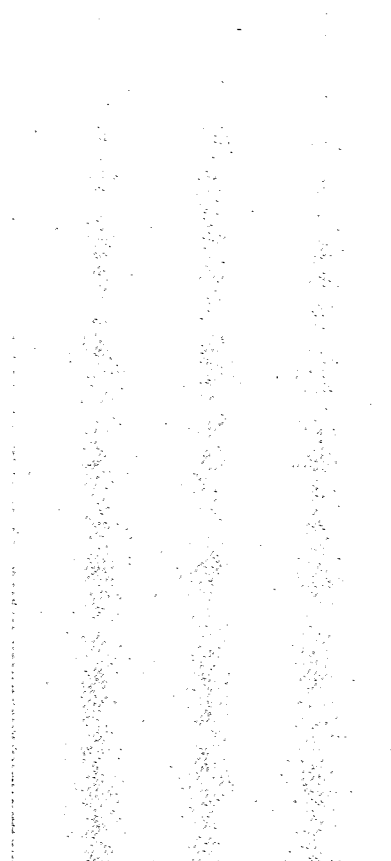
In general, the industry has been able to attract sufficient workers, especially immigrants. However, specialized skill shortages, particularly for computer numeric controlled (CNC) production processes and the manufacture of high-quality upholstery furniture, continue to exist. In addition, high turnover in some lower-skilled jobs has occurred.

In both Canada and the U.S., formal human resources practices, such as performance evaluation, tend to be weak compared with those in other manufacturing industries, but are generally more developed in the larger companies. Management sophistication in this industry increases with company size. Small firms tend to be owned by entrepreneurs having manufacturing backgrounds but less expertise in other functions. Overall, the U.S. industry has stronger marketing management skills.

**Canadian furniture
manufacturing is
25% unionized**

**Workers train informally,
on the job**

**Labour is available for most
jobs — except computer
control and fine upholstery**



Public Policy Governing the Industry

Horizontal policies and regulations of greatest significance to this industry are tariffs, pollution standards, consumer protection and labelling requirements.

**FTA eliminated Canadian
tariffs as high as 15%**

The tariff rates levied by Canada on most household furniture imports from nations having Most Favoured Nation (MFN) status with it in 1988 ranged from 9.2 percent to 15 percent, compared with 2.4 percent to 7.5 percent assessed by the U.S. on comparable goods. Under the FTA, the tariffs on furniture traded between Canada and the U.S. were eliminated in five annual, equal stages from January 1989 to January 1993. This loss of tariff protection was one of the largest faced by any manufacturing industry; it forced Canadian household furniture firms to make significant and rapid adjustments to improve their competitiveness in domestic markets and also to take a greater interest in becoming export-ready to seek new markets. Part of the industry's problem in adjusting to the FTA was due to the faster phase-out of Canadian tariffs on finished furniture than on inputs imported from the United States. The tariffs on input materials were originally scheduled to be eliminated over a 10-year period. However, the phase-out period was ultimately reduced to seven years through the accelerated tariff elimination provisions of the FTA. Since materials and supplies are the greatest cost factor (49.2 percent of 1994 industry shipments), access to competitively priced inputs are critical to a firm's success.

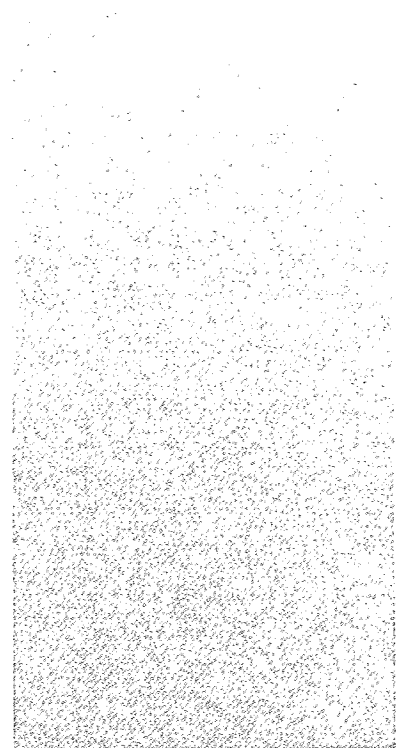
With the implementation of the NAFTA in 1994 and the establishment of the World Trade Organization (WTO) in 1995, replacing the General Agreement on Tariffs and Trade and incorporating the results of seven years of Uruguay Round multilateral trade negotiations, the industry faces further tariff reductions. The real impact of the tariff protection decline will depend on current and projected trade volumes. Under the NAFTA, some tariffs between Canada and Mexico will be eliminated in five annual stages, while the remainder will be phased out in 10 stages, beginning January 1, 1994. The cuts under the WTO will reduce Canadian and U.S. MFN household furniture tariffs by an average of one third over five years starting January 1, 1995. Tariffs on most input materials will also fall by an average of one third by the year 2000.

There are currently no significant non-tariff barriers in Canada's key export markets. However, environmental and other standards may become a major impediment to international trade.

The Canadian industry faces pollution control regulations similar to those of the U.S. and most western European countries. However, manufacturers in Mexico and many Far East countries face less stringent requirements or no requirements at all, which affords them a cost/price advantage. According to a 1991 U.S. General Accounting Office study (*U.S.-Mexico Trade: Report to the Chairman, Committee on Energy and Commerce, House of Representatives*), California's stringent air pollution standards have led a number of U.S. furniture companies to relocate to Mexico. The NAFTA side rules on the environment are aimed at ensuring the proper enforcement of existing regulations.

**Canada faces no
non-tariff barriers . . .**

**. . . but Mexico has far fewer
environmental controls**



**Flammability program
harmonized with U.S.**

Consumer protection regarding household furniture was augmented in 1986 when, at the federal government's invitation, the industry implemented a voluntary Upholstered Furniture Action Council (UFAC) flammability program to increase the fire safety (cigarette ignition resistance) of upholstered furniture. Administered by the CCFM, the program is completely harmonized with the U.S. UFAC program. In 1994, the U.S. Consumer Product Safety Commission launched a review of the U.S. UFAC program and a feasibility study on open flame ignition resistance (i.e. matches) for upholstered furniture. Recommendations are expected in early 1997.

In Canada, the quality and safety of furniture made in compliance with the UFAC program needs to be better communicated to retailers and consumers. A CCFM-Health Canada task force is examining this issue.

**Foreign goods sold in
Canada lack bilingual labels**

The industry has complained frequently that imported goods often do not meet Canadian labelling requirements. The lack of French language on labels affixed to imported goods is the most common problem. By evading these requirements, foreign exporters gain a cost/price advantage.

Government Support Mechanisms

**Federal and provincial
support has helped the
furniture industry ...**

... acquire information

... attend trade shows

**... upgrade design, quality
and productivity**

The federal government has undertaken a number of activities tailored to the industry's specific needs, ranging from special activity grants and contributions, to providing statistics and other information to support sound business decisions. For example, the Department of Foreign Affairs and International Trade, in partnership with Industry Canada, aids in international market development through trade shows, buyers' missions, market studies and education seminars. About 75 organizations received financial support under Industry Canada's 1994-96 Furniture Sector Campaign aimed at increasing competitiveness by sharing association and company costs to upgrade design, quality and productivity.

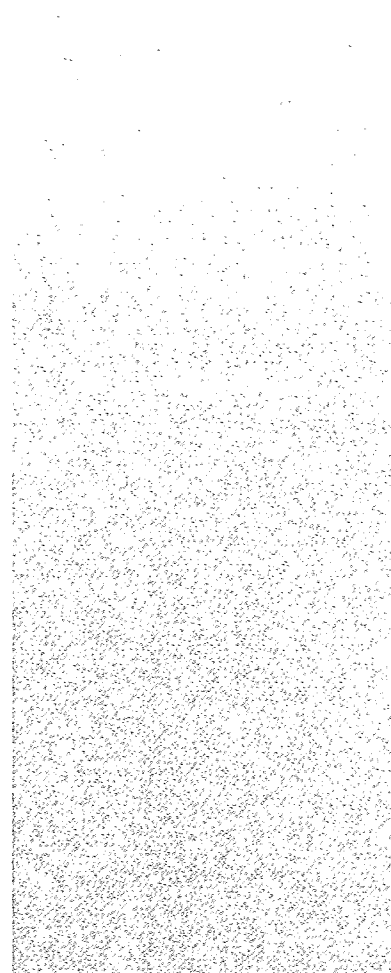
In 1991, supported by Human Resources Development Canada (HRDC), furniture industry representatives created an Industrial Adjustment Service Committee to analyze critical human resources planning factors and review training system adequacy to meet future requirements. An in-depth study of present and future labour market challenges by Ernst & Young followed, and the report (*Today's Challenges Tomorrow's Realities: Towards a Human Resource Strategy in the Canadian Furniture Manufacturing Industry*) was released in 1994.

**... analyze human
resource needs**

In the early 1990s, Industry Canada and members of the furniture and wood processing industries championed the transfer of a German university curriculum (Fachhochschule Rosenheim) to address a major scarcity in wood processing engineers needed by these industries. In March 1995, HRDC contributed to a privately administered fund, whose interest earnings were to be used to aid the University of British Columbia in adopting this curriculum. The university began accepting students in the fall of 1995 and will initially graduate about 50 students per year. In addition, New Brunswick and British Columbia are developing college-level programs to link into the University of British Columbia program.

**... develop higher levels of
training and achievement**

Active provincial assistance includes Ontario government funding for the past 20 years to the Ontario Furniture Manufacturers Association (OFMA) for the annual Trillium Awards to recognize design and marketing achievement. As well, the OFMA received \$300 000 in 1993 from the Ontario government's Sector Partnership Fund to develop an industrial policy framework. In 1993, the Quebec government agreed to contribute \$1 million over five years to L'Association des fabricants de meubles du Québec to implement an export marketing campaign. In 1994, the Quebec government introduced a design tax credit, which enables small companies in the furniture and fashion industries to deduct up to 40 percent of design costs, and large companies up to 20 percent.

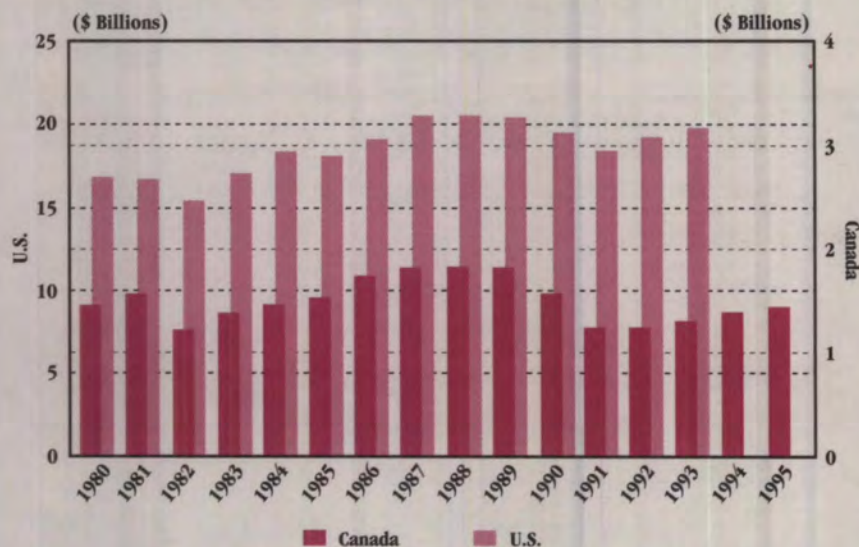


The furniture industry
has recovered from FTA
and recession setback
to achieve 3.8% annual
growth...

2.4 Performance

The value (as measured in constant 1986 dollars) of Canadian shipments rose strongly between 1983 and 1987, from \$1.38 to \$1.82 billion. This was followed by a decline coinciding with a deep recession and the introduction of the FTA. This decline was so dramatic that virtually all gains were lost, resulting in a trough-to-trough (1982–91) real growth averaging only 0.2 percent per year. Since 1991, real shipments have begun to pick up to reach \$1.44 billion in 1995, reflecting strong exports to the U.S. From 1991 to 1995, real industry shipments grew by 3.8 percent per year (Figure 4).

Figure 4. Comparison of Canadian and U.S. Household Furniture Industry Shipments
(constant 1986 Canadian dollars)



Source: Statistics Canada, Catalogue No. 35-251; U.S. Department of Commerce, *Census of Manufacturers, 1992*, and *U.S. Industrial Outlook, 1993*.

In contrast, U.S. industry real shipments grew at an annual average rate of 2 percent between 1982 and 1991, and 3.8 percent from 1991 to 1993. Because of much weaker growth, Canada's share of Canada-U.S. real shipments combined fell from an already low 7.3 percent in 1982 to 6.3 percent in 1991 and 6.2 percent in 1993.

Canadian industry profit margins following the recession of the early 1980s remained positive until 1990. The industry's financial performance has since deteriorated substantially (see Annex A for statistics).

Average annual capital and repair expenditures, in current dollars, amounted to \$40 million between 1982 and 1994 — \$25.7 million in new capital investments and \$14.3 million in repairs. These capital expenditures represented only 1.6 percent of shipment value over the 12-year period, compared with expenditures of 5.3 percent for Canada's overall manufacturing sector. Machinery and equipment costs are relatively modest in the furniture industry, but are growing. Between 1982 and 1992, capital investment per household furniture production worker, in current dollars, averaged only \$1114 a year in Canada, compared with the equivalent of C\$1732 in the United States.

Technology innovation in the household furniture industry both in Canada and other countries generally originates with machinery and equipment suppliers. Much of this research and development work is done outside Canada, notably in Europe. Until fairly recently, furniture manufacturing technologies

**... but U.S. has grown
more strongly; therefore
Canada's share diminishes**

**Capital investments are
lower in Canada than in U.S.**

R&D is low



were considered quite mature, and advances were marginal. Recent research and development activities have been directed primarily at increasing speed and efficiency. Similarly, the industry depends largely on outside companies for research and development on materials.

**Large Canadian firms have
modern equipment that
smaller firms lack**

Most large Canadian household furniture firms have state-of-the-art machinery and equipment. For a number of reasons, including economic and market factors, the rate of diffusion of new technologies is much slower in smaller firms.

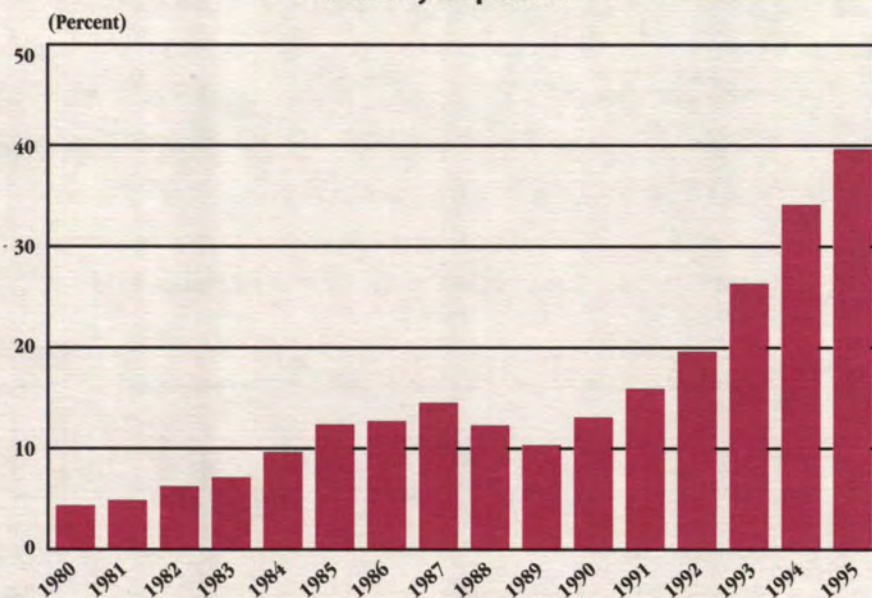
There are no basic differences in the technologies used by the Canadian and U.S. household furniture industries. In contrast, western European firms tend to use more advanced labour-saving product and process technologies to offset declining supplies of hard and soft woods and higher labour costs.

International trade over the past decade, and particularly since the implementation of the FTA, has become a more important activity of the Canadian industry. Trade liberalization has resulted in growing import pressures, but at the same time has created new export opportunities for firms that were able to adjust.

Exporting has been the major bright spot for the Canadian industry. Canadian export orientation (exports as a share of shipments) increased from 6.2 percent in 1982 to 14.5 percent in 1987 and surged to 39.8 percent in 1995 (Figure 5). By and large, successful exporters have generally focussed on furniture of innovative design and good quality.

Exports are growing rapidly

Figure 5. Export Share of Canadian Household Furniture Industry Shipments



Source: Statistics Canada, Catalogue Nos. 65-004 and 35-251; TIERS CD-ROM.

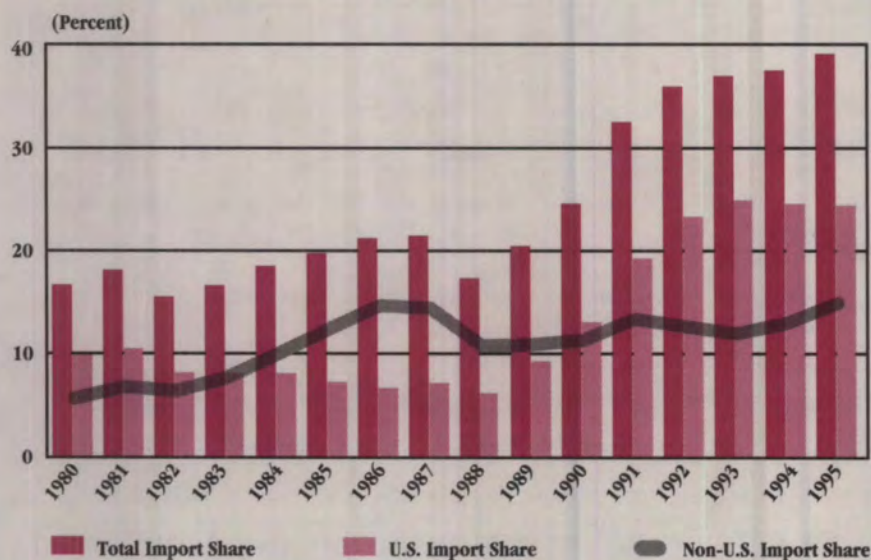
Canadian current-dollar exports of household furniture expanded from \$65.6 million in 1982 to \$727.6 million in 1995, an increase of 1003 percent. Exports of wooden furniture increased from \$39.1 million to \$545.8 million, a gain of 1296 percent, compared with a gain of 441 percent for upholstered furniture (from \$16.7 million to \$90.4 million) and 833 percent for other furniture products (from \$9.8 million to \$91.4 million).

**Import penetration has
doubled since 1982**

Canada's main export market has always been the United States (95.7 percent in 1995). Many Canadian exporters now consider the U.S. market as a natural extension of their domestic market. Factors that keep the U.S. market in the foreground include its size, proximity and preferential tariffs. Factors that discourage ventures into other markets include overseas shipping costs, tariff barriers and a lack of knowledge about distant markets.

Import penetration of the Canadian market (imports as a share of the market) has more than doubled from 15.2 percent in 1982 to 38.7 percent in 1995. Following implementation of the FTA, the U.S. has supplied virtually the whole increase in import penetration. Imports from other countries currently hold 14.6 percent of the Canadian market, compared with 11 percent in 1988 (Figure 6).

Figure 6. Import Penetration of the Canadian Household Furniture Market



Source: Statistics Canada, Catalogue Nos. 65-004, 65-007 and 35-251; TIERS CD-ROM.

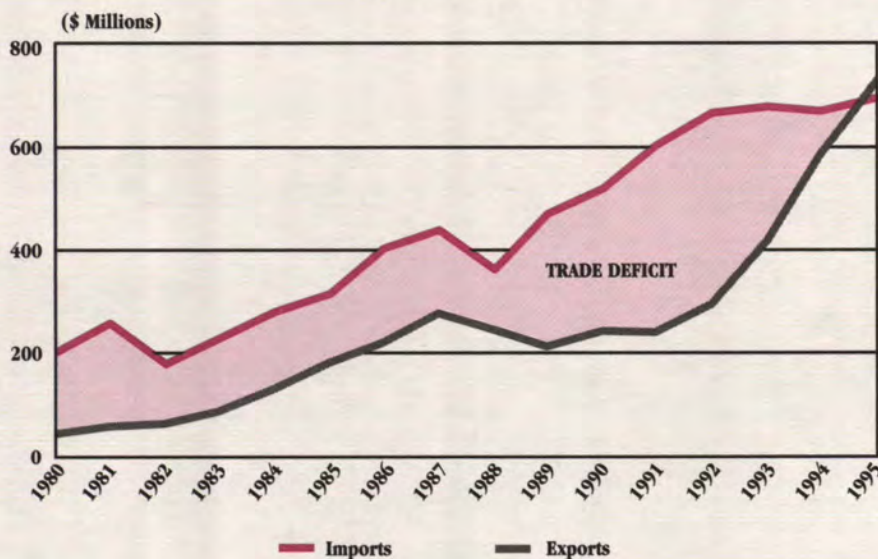
Current-dollar imports of household furniture into Canada increased from \$176.3 million in 1982 to \$692.7 million in 1995, a gain of 294 percent. Imports of upholstered furniture jumped from \$18.1 million to \$222.7 million, an increase of 1130 percent. Imports of wooden products reported a gain of 249 percent from \$93.3 million to \$325.3 million, while imports of other furniture products grew by 123 percent from \$64.8 million to \$144.7 million.

In 1995, the U.S. contributed 62.2 percent of Canadian imports. High-end goods mostly from Italy provided 13.5 percent, and low-end goods mostly from Taiwan and China supplied 24.3 percent.

The Canadian trade balance in current dollars between 1982 and 1994 was constantly negative. Wide annual fluctuations ranged from a 1992 high of \$370.3 million to a 1994 low of \$81.8 million. In 1995, for the first time ever, a trade surplus of \$35 million was generated because of a strong export performance (Figure 7).

Canada achieved trade surplus in furniture during 1995

Figure 7. Canadian Trade Balance in Household Furniture
(current dollars)



^a Data for 1988 and after are reported by code groupings under the Harmonized Commodity Description and Coding System.

Source: Statistics Canada, Catalogue Nos. 65-004 and 65-007; TIERS CD-ROM.

**Wood furniture contributes
to Canada's trade balance**

The trade balance in wooden household furniture was in a deficit position from 1982 to 1992, then switched to a surplus, reaching a peak of \$220.5 million in 1995. The upholstered products trade balance went from a deficit in 1982–83 to a surplus in 1984–87, reverting to a deficit reaching \$205.1 million in 1992 before moderating to a deficit of \$132.3 million in 1995. The “other” household furniture products deficit varied over the 1982–95 period, but showed no definite trend, amounting to a deficit of \$53.2 million in 1995.

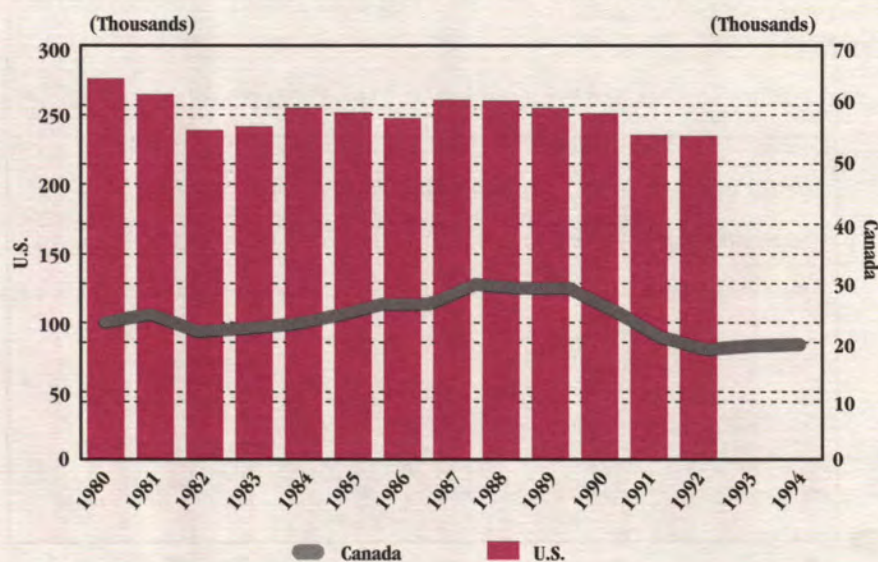
Canada's trade balance with the U.S. moved from a deficit in 1982–83 to a surplus in 1984–88, switching to a deficit in 1989–93, reverting to a surplus and reaching a peak of \$265.6 million in 1995. The trade deficit with the European Union has fluctuated widely; it stood at \$77.5 million in 1995, well below the peak of \$139.8 million in 1986. Canada's trade deficit with Asia has jumped from \$31.8 million in 1982 to \$143.6 million in 1995.

Human Resources

Employment in the Canadian industry fell by about 1.5 percent a year between 1982 and 1992 (from 21 725 to 18 721), compared with a 0.2 percent annual decline among U.S. counterparts (from 237 600 to 233 600). Canada's share of Canada-U.S. total employment fell from 8.4 percent in 1982 to 7.4 percent in 1992 (Figure 8).

**Employment in Canada
echoes U.S., but weaker**

Figure 8. Comparison of Employment Levels in the Canadian and U.S. Household Furniture Industries

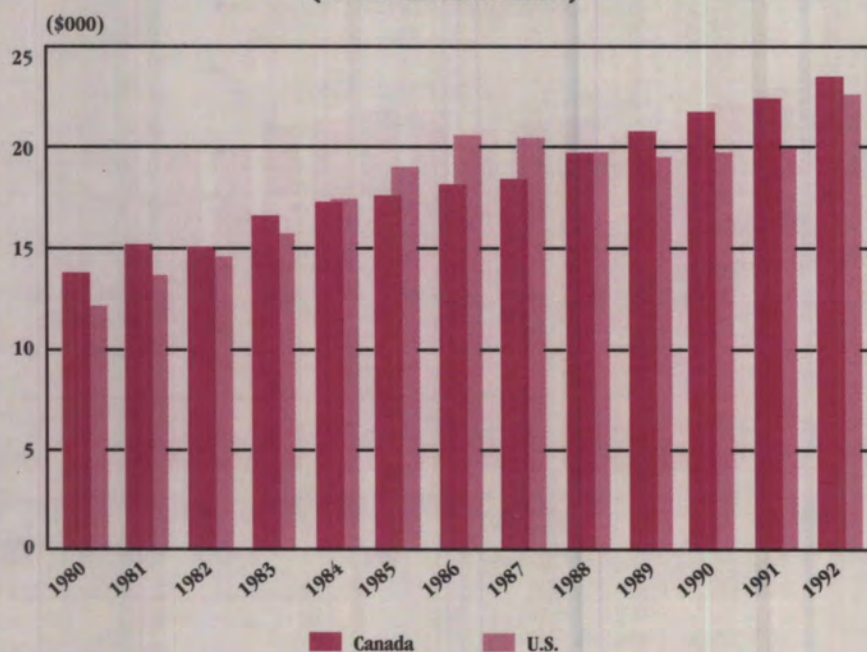


Source: Statistics Canada, Catalogue No. 35-251; U.S. Department of Commerce, *Census of Manufacturers*, 1992.

In both Canada and the United States, production workers make up about 85 percent of the household furniture labour force, while management, administration and sales functions account for the other 15 percent. Current wages and salaries per employee, expressed in Canadian dollars, increased at

about the same annual rates over the 1982–92 period: 4.6 percent for Canada and 4.5 percent for the U.S. (Figure 9). In 1992, Canadian production workers made \$10.31 per hour (excluding fringe benefits), compared with the equivalent of C\$10 in the United States. However, average annual salary costs of non-production employees were lower in Canada than in the United States (\$35 809 versus C\$40 845).

Figure 9. Comparison of Wages and Salaries per Employee in the Canadian and U.S. Household Furniture Industries
(current Canadian dollars)

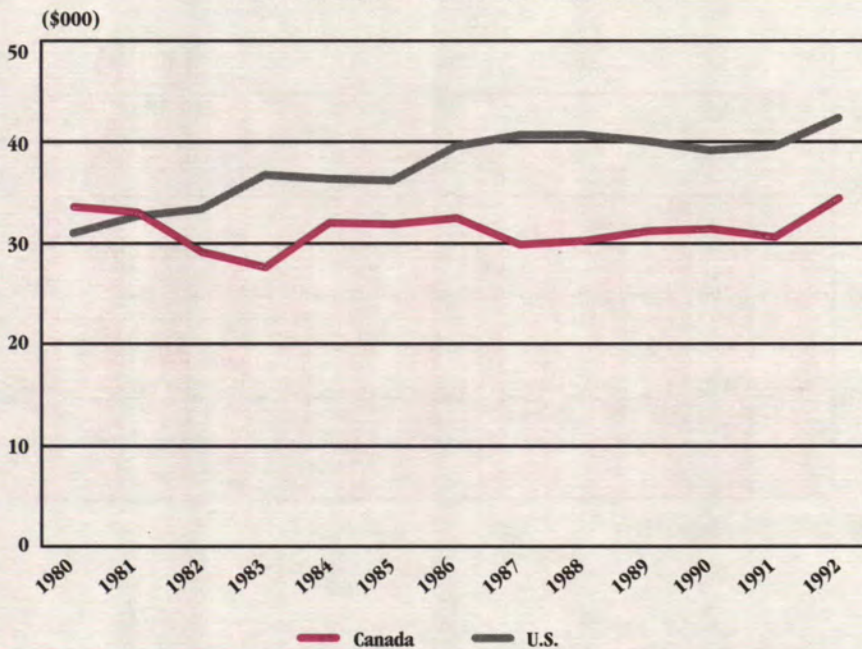


Source: Statistics Canada, Catalogue No. 35-251; U.S. Department of Commerce, *Census of Manufacturers*, 1992.

Although the Canadian industry has restructured, its productivity continues to trail that of its U.S. counterpart. U.S. labour productivity, as measured by value-added per employee in constant 1986 dollars, was 21.3 percent higher than Canadian labour productivity in 1982, and this lead increased to 29.6 percent by 1991, but fell to 23.1 percent in 1992 (Figure 10). The higher productivity level is due in part to higher capital investment. The larger scale of U.S. plants is also a factor.

**Canadian productivity falls
below U.S. level**

Figure 10. Comparison of Productivity Levels in the Canadian and U.S. Household Furniture Industries
(constant Canadian dollars per employee)



Source: Statistics Canada, Catalogue No. 35-251; U.S. Department of Commerce, *Census of Manufacturers*, 1992.

3 CHANGING CONDITIONS AND INDUSTRY RESPONSE

§.1 Investment and Financing

**The furniture industry has
problems finding capital**

The industry, particularly among smaller firms, has long encountered problems in raising capital to keep pace with technology, largely because of lower-than-average profit margins and investment returns.

§.2 Trade

**Canada has lost more
than 20% of its domestic
market ...**

In 1995, the Canadian industry controlled only 61.3 percent of its domestic market versus 84.8 percent in 1982. Import penetration is particularly high in the upholstered furniture subsector.

**... but exports are
six times the 1982 level**

Declining domestic demand, growing imports and foreign market tariff reductions have encouraged the industry to move away from a domestic orientation toward a North American orientation. Canadian manufacturers exported 39.8 percent of output in 1995, compared with only 6.2 percent in 1982. The industry was particularly successful in exporting wooden furniture.

§.3 Technology

**Large firms back new
technology to help
them compete for
demanding customers**

Competitive conditions are pushing more manufacturers, primarily the larger ones, to use both "hard" (i.e. production) technologies and "soft" technologies (all others) to achieve production flexibility to satisfy increasingly demanding consumers. The benefits are lower costs/higher productivity, consistently higher quality and more efficient use of raw materials (see Annex C for a review of hard and soft technologies applicable to this industry).

3.4 Human Resources

A growing number of Canadian firms are placing greater emphasis on design, product quality and customer services to offset high labour costs. Some firms have increased productivity by modernizing their operations and/or rationalizing and specializing production. Several firms have successfully introduced newer forms of work organizations such as self-managed work groups, which have increased productivity levels. Other firms have invested in bar coding technologies to improve efficiency.

As part of the 1994 study mentioned earlier, Ernst & Young explored potential skill gaps in the Canadian furniture sector over the next five years. In general, the occupations where the greatest skill gaps lie are likely to be direct production management, general management, and administrative and sales functions, followed by basic production occupations. Supported by HRDC and Industry Canada, the industry is developing an action plan based on the study's recommendations. Without skill improvement and computer literacy, the industry will have difficulty in introducing enhanced productivity measures such as just-in-time (JIT), bar coding and other new technologies.

Reliable information on the gap in skills in the U.S. and European household furniture industries is not available. However, according to some Canadian manufacturers, the two Canadian schools providing dedicated furniture skills training are not as well equipped as the leading U.S. and European schools.

**Canadian firms' strategies
emphasize design, quality,
customer services**

**Management needs
skill development**



3.5 Sustainable Development

**Clean air laws force
changes to solvents, paints
and wood input materials**

Although the manufacturing processes used in making household furniture do not give rise to serious pollution problems, the industry has had to take a number of corrective measures to comply with increasingly stringent federal, provincial and local regulations concerning clean air. The regulation pertaining to volatile organic compounds (VOCs) in solvents and paint coatings has had the most impact on wooden household furniture manufacturers. Another important issue concerns formaldehyde emissions from some materials used in the construction of furniture, notably particleboard.

While the industry is paying more attention to reducing the environmental impact of its products, notably by reducing waste, improving the energy efficiency of its processes and by using more recycled material for packing and packaging, it recognizes there is still more to do.

3.6 Currency Exchange Rates

In response to exchange rate fluctuations, furniture manufacturers have continued to focus on containing their costs and enhancing productivity.

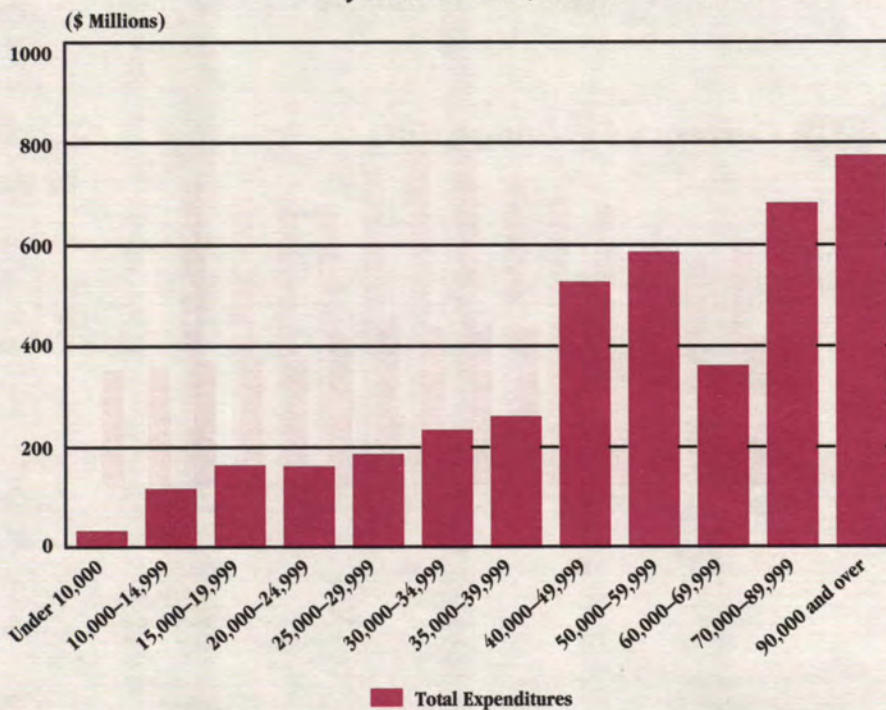
4 GROWTH PROSPECTS FOR THE INDUSTRY

4.1 Demand Outlook

The need to furnish a new apartment/home or to replace existing furniture drives household furniture demand. Household furniture expenditures generally increase with household size and income, and are higher for homeowners than for tenants. High income earners spend significantly more on household furniture (Figure 11). The customer base, mainly women, tend to be fairly sensitive to price-value relationships, are discriminating and are often individualistic.

**The typical customer
is a discriminating,
price-conscious woman**

Figure 11. Canadian Consumer Expenditures on Household Furniture, by Income Level, 1992



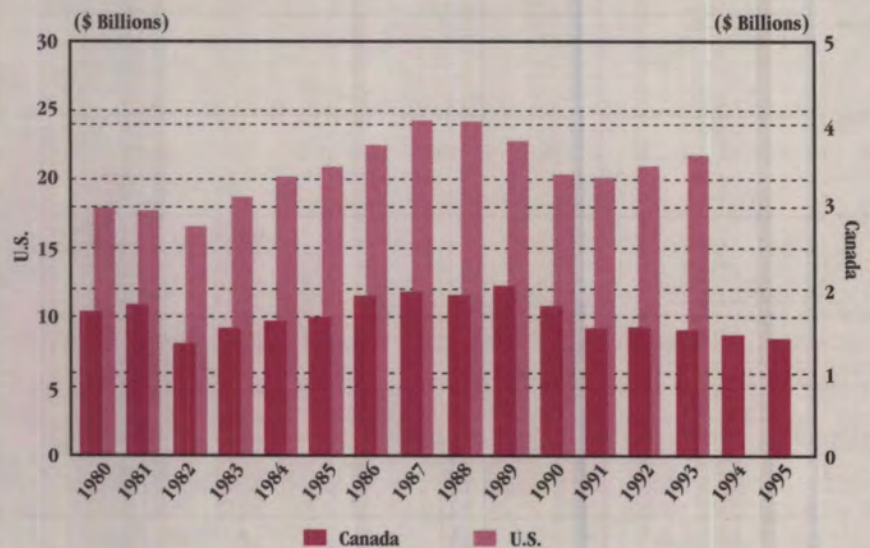
Source: Statistics Canada, Catalogue No. 62-555.

**Demographic and
economic pressures slow
Canadian market ...**

In the short term, market demand for household furniture is very susceptible to economic shifts, including factors such as interest and unemployment rates. Over the longer term, market demand is largely dependent on household formation rates, housing starts and income growth.

The Canadian market for household furniture in constant 1986 dollars rose from \$1.34 billion in 1982 to a peak of \$2.04 billion in 1989, and has since declined to \$1.41 billion in 1995 (Figure 12). The market has grown by 1.5 percent annually on a trough-to-trough basis (1982–91). In contrast, the U.S. market has expanded at an annual rate of 2.2 percent between 1982 and 1991.

Figure 12. Comparison of Canadian and U.S. Household Furniture Markets
(constant 1986 Canadian dollars)



^a Data are reported by code groupings under the Harmonized Commodity Description and Coding System for 1988 and after for Canada and for 1989 and after for the U.S.

Source: Statistics Canada, Catalogue Nos. 65-004, 65-007 and 35-251; TIERS CD-ROM; U.S. Department of Commerce, *Census of Manufacturers*, 1992; U.S. Imports for Consumption; U.S. Exports publications, National Trade Data Bank.

The share of Canadian shipments in the joint Canada–U.S. market fell from 6.7 percent in 1982 to 5.6 percent in 1993. Reasons for the decline in the Canadian share include a more severe industry shakeout in Canada than in the U.S. following implementation of the FTA and slower growth in the Canadian market due to a more severe recession.

Over the 1996–2005 period, the Canadian market is forecast to grow by 1 percent a year on average, lower than the consumer expenditure growth projections of 1.5 percent. Product niches offering above-average growth will include furniture for the elderly and home entertainment centres. As well, the popularity of ready-to-assemble (RTA) furniture is expected to continue.

Market segments to watch include growing numbers of singles, newly formed families, “empty nesters” who are moving, and new immigrants (see Annex D for more information on demand outlook).

Over the next several years, U.S. market demand is forecast to increase by 2–3 percent annually. Canada’s current share of this market is small (1.5 percent), leaving considerable room for expansion.

Several foreign markets are also opening in response to tariff reductions following implementation of the WTO and the NAFTA. The European Union, currently Canada’s second largest export market, is expected to offer the best hope for aggressive exporters, particularly for high-end furniture. Asia Pacific, notably Japan, is also expected to provide a market for Canadian high-end furniture, although products for this market may require size and design modifications. Tariff elimination under the NAFTA coupled with expected economic and demographic growth should also improve the climate for future export to Mexico.

Canada’s North American market share declined in the slow-growth period after FTA

Dramatic change is unlikely

Niche markets offer pockets for growth

Growth in U.S. and lowered tariffs worldwide present opportunities for Canadian firms

Asia Pacific and Latin America represent untapped potential for Canadian exports. Immigrants from these areas may also help to provide crucial links (language, customs, business practices) that can be exploited for increased sales.

**Retailers and buying groups
now have the upper hand**

Over the past decade, negotiating power has clearly shifted away from furniture manufacturers to retailers and buying groups. The largest furniture retail chain in Canada is about the same size as the largest Canadian manufacturer, while the largest buying group is about twice the size of the biggest manufacturer.

**Wal-Mart syndrome
invades the furniture
retail marketplace**

Furniture retailing is likely to undergo a shakeout as businesses become more sophisticated and competitive. Less competitive independents are likely to lose a significant share of the market. Traditional department stores may lose share as discounters like Wal-Mart grow (see Annex E for more information on retailing).

**Quality, design and
marketing issues displace
past concerns about
raw materials, tariffs and
transportation costs**

In the past, labour costs, access to raw materials, tariff rates and transportation costs were critical to competitiveness. While these factors will continue to play an important role, quality, design and marketing strategies will take on added importance in the future.

Canadian manufacturers have a reputation for quality not yet being used effectively in marketing their product. With case goods in particular, retailers have traditionally stripped off the manufacturer's brand name and have replaced it with their own to gain the customer's allegiance.

While Canadian furniture has not traditionally been known for innovative design, it is receiving more emphasis, particularly in Quebec. Furniture design development can be a high-risk investment, as continually changing consumer preferences make it difficult to predict consumer reaction to new designs.

To offset these risks, the Canadian industry needs to strengthen marketing. Most firms are primarily oriented to production and do not consciously pursue marketing objectives and strategies. The U.S. industry is generally more oriented toward marketing.

The household furniture industry worldwide tends to be labour intensive and will remain so for the foreseeable future, despite continuing introduction of more automated production technologies. The prospects for employment growth in the Canadian industry are modest at best. Overall, the number of Canadian firms will not grow and may decline further. It is probable that firms will become more clustered at the small and large ends of the spectrum, with fewer in the middle.

4.2 Current Industry Strengths and Weaknesses

The Canadian household furniture industry over the years has proven to be a resilient manufacturing sector, capable of adjusting to significant market changes. To redress declining domestic demand coupled with growing import pressures in the late 1980s and early 1990s, Canadian household furniture companies took a number of actions. One was to reorient marketing efforts toward the U.S., where the industry has achieved significant success.

The Canadian industry has a reputation for quality, although this is more apparent to the retailers that act as an intermediary than to the customer.

Many smaller Canadian firms have used their size to advantage by adopting flexible manufacturing systems to meet orders from small buyer groups in Canada and abroad. These systems minimize shorter production-run costs.

**Mid-sized Canadian firms
most likely to feel the pinch**

**The furniture industry
has proved resilient and
responsive to change**

**"The furniture industry
is part of a dramatic re-
definition of the relationship
between the producers of
goods (the manufacturers),
the distributors (the retail-
ers), and their clients (the
customer)."**

**— Serge Racine, Chairman
of the Board, Shermag Inc.**

The industry needs ...**... unique design****... higher productivity****... lower costs****... improved marketing****... a stronger association**

A key challenge is the shortage of unique product design. Much household furniture is marketed as a commodity rather than as a fashion item. As well, the Canadian industry operates at lower productivity than its U.S. competitors and incurs higher wage costs using essentially the same technologies. Western European firms' manufacturing costs are lower than those in North America because of higher investment in labour-saving technologies and a greater use of board materials. More analysis, through benchmarking or similar studies, is needed to identify specific areas for improvement.

Overall, the Canadian industry needs to improve marketing skills. Finally, the effectiveness of the national association has been affected by regional rivalries.

4.3 Future Competitive Threats

The industry is highly cost sensitive and therefore highly susceptible to exchange rate movements. Further, the industry must prepare for an increasingly competitive environment.

Dangers lurk in ...**... currency exchange rates**

A rising Canadian dollar value relative to the U.S. currency would put severe pressures on domestic producers, as occurred during the mid-1980s to early 1990s. The Canadian industry would reduce its vulnerability to currency fluctuations by seeking to outperform its U.S. counterpart in the areas of productivity growth and cost containment.

**... Mexican, Asian
and European imports**

The other threat arises from reduced tariffs for furniture imports from Mexico (under the NAFTA), Europe and Asia (under the WTO). Both domestic and U.S. markets will be affected, particularly in high-priced furniture from Europe, as well as furniture components and low-priced furniture from Mexico and Asia.

These competitive threats are even more important in view of the forecasts for relatively slow domestic growth. Market share gains, primarily through exports to the vast U.S. market, could be a main expansion source. Success on this front is critical to offset the increasing penetration of foreign furniture goods in the Canadian market.

4.4 Future Opportunities

In terms of markets, Canadian producers need to examine niche market potential in their largest market, the United States, as well as in the European Union. They also need to assess the potential of rapidly growing markets in Asia Pacific (notably Japan) and Latin America.

In terms of products, niches to consider include environmentally sound products, along with furniture for the elderly and entertainment centres. Overall, the market potential of moving consumer perception of furniture from a commodity to a fashion item needs to be examined.

Compared with U.S.-made furniture, the Canadian product is acknowledged to be of higher quality, although this is still more apparent to retailers than to customers. Enhanced design is an important element that must be married with the already high quality of products to successfully market more Canadian furniture domestically and abroad.

Future markets include the U.S., the EU and Asia Pacific

Niches can be carved from shifts in demography and taste

Quality is Canada's edge on U.S. competitors

"Canadian-designed furniture...whether they're one-of-a-kind craft pieces, limited run articles from small producers or manufactured products from growing firms, they're steadily finding a niche in Canadian and international markets."

— Ottawa Interiors, January 1994

4.5 The Bottom Line

Framework for Action
will address issues
through consultation

The future of the Canadian industry depends on its ability to strengthen competitiveness by addressing its weaknesses; not doing so could lead to both production and job loss. In comparison with its U.S. counterpart, the weaknesses include, in particular, higher MFN tariffs on input materials, higher labour costs, lower capital investment, lower productivity, lagging design and marketing, and a weak national trade association.

These issues will be addressed in a forthcoming *Framework for Action*, to be developed after extensive consultations with industry stakeholders. Industry Canada hopes that this *Overview and Prospects* will provide a solid basis for jointly discussing and planning resolutions.

For further information concerning the subject matter contained in this overview, please contact:

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Annex A

COMPARATIVE STATISTICS: CANADIAN AND U.S. HOUSEHOLD FURNITURE INDUSTRIES

Table 1. Canadian Household Furniture Industry^a — Principal Statistics^b

	Plants (no.)	Production workers (000s)	Wages		Total employment (000s)	Salaries and wages		Total value-added	
			(current \$ mil.)	(constant ^c \$ mil.)		(current \$ mil.)	(constant ^c \$ mil.)	(current \$ mil.)	(constant ^c \$ mil.)
1978	N/A	19.3	205.4	335.4	22.8	260.9	451.4	428.4	741.2
1979	N/A	20.9	246.9	382.2	24.5	308.4	477.4	524.7	812.2
1980	N/A	19.6	251.9	354.3	23.3	320.7	451.1	556.3	782.4
1981	N/A	20.6	288.3	364.5	24.6	373.2	471.8	642.5	812.3
1982	874	19.5	254.6	294.0	21.7	326.5	377.0	517.0	597.0
1983	930	19.1	290.4	320.9	22.2	368.5	407.2	640.7	708.0
1984	949	19.7	312.8	331.4	22.9	395.7	419.2	690.6	731.6
1985	994	21.6	350.3	361.9	24.4	429.4	443.6	751.5	776.3
1986	1 035	23.9	402.3	402.3	26.4	479.2	479.2	856.1	856.1
1987	1 065	N/A	N/A	N/A	29.8	548.8	522.7	930.9	886.6
1988	1 157	26.4	484.3	441.5	29.1	573.0	522.3	961.3	876.3
1989	1 029	26.5	509.0	447.7	29.2	605.7	532.7	1 032.2	907.8
1990	1 078	22.6	453.7	383.2	25.3	549.5	464.1	937.9	792.2
1991	782	18.3	382.0	314.4	20.8	466.0	383.5	770.2	633.9
1992	659	15.9	339.1	281.2	18.7	439.4	364.3	775.1	642.7
1993	620	16.4	356.6	292.1	19.3	457.2	374.5	800.5	655.7
1994	578	16.7	362.5	293.1	19.5	461.2	372.8	855.3	691.4
1995	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A

^a Standard Industrial Classification (SIC) codes 2611, 2612 and 2619.^b Values are in Canadian dollars.^c At 1986 prices.

N/A = not available.

Source: Statistics Canada, unpublished data for 1978 to 1981, Catalogue No. 35-216 for 1982 to 1984 and Catalogue No. 35-251 for 1985 to 1994.

Table 2. Canadian Market For Household Furniture^a

	Canadian industry shipments		Canadian exports		Canadian imports		Canadian market ^b	
	(current \$ mil.)	(constant ^c \$ mil.)	(current \$ mil.)	(constant ^c \$ mil.)	(current \$ mil.)	(constant ^c \$ mil.)	(current \$ mil.)	(constant ^c \$ mil.)
1978	827.0	1 430.8	23.0	39.8	182.1	315.5	986.1	1 706.1
1979	1 006.5	1 558.1	35.1	54.3	201.4	311.8	1 172.8	1 815.5
1980	1 073.0	1 509.1	46.4	65.3	200.3	281.7	1 226.9	1 725.6
1981	1 236.1	1 562.7	60.0	75.9	254.4	321.6	1 430.5	1 808.5
1982	1 052.6	1 215.5	65.6	75.8	176.3	203.6	1 163.3	1 343.3
1983	1 246.6	1 377.5	88.8	98.1	224.9	248.5	1 382.7	1 527.9
1984	1 377.3	1 459.0	131.7	139.5	276.3	292.7	1 521.9	1 612.2
1985	1 476.7	1 525.5	181.7	187.7	311.9	322.2	1 606.9	1 660.0
1986	1 737.5	1 737.5	219.7	219.7	400.0	400.0	1 917.8	1 917.8
1987	1 906.2	1 815.4	276.3	263.1	435.9	415.1	2 065.8	1 967.4
1988	2 000.7	1 823.8	244.4	222.8	359.2	327.4	2 115.5	1 928.4
1989	2 066.4	1 817.4	212.2	186.6	466.8	410.6	2 321.0	2 041.3
1990	1 856.5	1 568.0	242.0	204.4	515.8	435.6	2 130.3	1 799.2
1991	1 505.4	1 239.0	239.7	197.3	600.3	494.1	1 866.0	1 535.8
1992	1 496.2	1 240.6	293.7	243.5	664.0	550.6	1 866.5	1 547.7
1993	1 591.4	1 303.4	418.1	342.2	676.1	553.7	1 849.5	1 514.7
1994	1 717.4	1 388.4	585.6	473.4	667.4	539.5	1 799.2	1 454.5
1995	1 827.0	1 438.6	727.6	572.9	692.7	545.4	1 792.1	1 411.1

^a Values are in Canadian dollars.^b Industry shipments less exports and plus imports.^c At 1986 prices.

Source: Statistics Canada, unpublished data and Catalogue No. 35-216, 35-251, 65-004 and 65-007.

Table 3. U.S. Household Furniture Industry^a — Principal Statistics^b

	Plants (no.)	Production workers (000s)	Wages		Total employment (000s)	Salaries and wages		Total value-added	
			(current \$ mil.)	(constant ^c \$ mil.)		(current \$ mil.)	(constant ^c \$ mil.)	(current \$ mil.)	(constant ^c \$ mil.)
1978	N/A	249.6	2 059.3	3 006.3	289.7	2 691.8	3 929.6	5 260.8	7 680.0
1979	N/A	246.2	2 135.8	2 909.8	286.7	2 818.7	3 840.2	5 453.5	7 429.8
1980	N/A	234.8	2 156.8	2 669.3	275.3	2 864.2	3 544.8	5 506.9	6 815.5
1981	N/A	225.3	2 267.4	2 621.3	263.9	3 002.2	3 470.8	5 916.7	6 840.1
1982	4 573	202.4	2 090.9	2 305.3	237.6	2 804.3	3 091.8	5 572.7	6 144.1
1983	N/A	207.2	2 319.7	2 505.1	240.4	3 065.9	3 310.9	6 290.3	6 793.0
1984	N/A	218.6	2 573.4	2 694.7	254.1	3 419.2	3 580.3	6 837.9	7 160.1
1985	N/A	214.7	2 617.3	2 659.9	250.6	3 490.5	3 547.3	6 970.8	7 084.2
1986	N/A	212.6	2 757.0	2 757.0	246.5	3 647.9	3 647.9	7 616.2	7 616.2
1987	4 775	222.9	3 026.5	2 952.7	259.9	4 003.6	3 906.0	8 321.5	8 118.5
1988	N/A	223.0	3 149.2	2 954.2	259.4	4 155.8	3 898.5	8 584.3	8 052.8
1989	N/A	217.4	3 118.2	2 824.5	254.0	4 179.3	3 785.6	8 510.8	7 709.1
1990	N/A	213.7	3 118.5	2 750.0	250.2	4 227.5	3 728.0	8 546.8	7 536.9
1991	N/A	199.3	2 991.9	2 577.0	234.3	4 066.7	3 502.8	8 329.8	7 174.7
1992	4 669	199.4	3 211.7	2 724.1	233.6	4 367.8	3 704.7	9 174.8	7 781.9
1993	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
1994	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A

^a Standard Industrial Classification (SIC) codes 2511, 2512, 2514, 2517 and 2519.^b Values are in U.S. dollars. For the analytical portion of this document, the values in constant dollars have been converted into Canadian dollars by using the following purchasing power parity indices: 1978 = 1.22, 1979 = 1.23, 1980 = 1.25, 1981 = 1.26, 1982 = 1.29, 1983 = 1.30, 1984 = 1.29, 1985 = 1.28, 1986 = 1.28, 1987 = 1.30, 1988 = 1.31, 1989 = 1.32, 1990 = 1.30, 1991 = 1.29 and 1992 = 1.27^c At 1986 prices.

N/A = not available.

Source: U.S. Department of Commerce Catalogue No. MC92-1-25A(P).

Table 4. U.S. Market for Household Furniture^a

	U.S. industry shipments		U.S. exports ^b		U.S. imports ^b		U.S. market ^c	
	(current \$ mil.)	(constant ^d \$ mil.)	(current \$ mil.)	(constant ^d \$ mil.)	(current \$ mil.)	(constant ^d \$ mil.)	(current \$ mil.)	(constant ^d \$ mil.)
1978	10 416.8	15 207.0	124.6	182.0	580.0	846.7	10 872.2	15 871.8
1979	10 706.3	14 586.2	141.2	192.4	717.8	978.0	11 282.9	15 371.8
1980	10 889.1	13 476.6	74.7	92.5	781.8	967.6	11 596.2	14 351.7
1981	11 486.6	13 279.3	230.3	266.2	904.2	1 045.3	12 160.5	14 058.4
1982	10 840.3	11 951.8	210.8	232.5	1 008.8	1 112.3	11 638.3	12 831.6
1983	12 185.4	13 137.6	171.0	184.7	1 320.6	1 426.2	13 315.0	14 379.1
1984	13 588.7	14 229.0	157.2	164.6	1 499.2	1 569.9	14 930.8	15 634.3
1985	13 917.3	14 143.6	127.8	129.9	2 267.4	2 304.3	16 056.9	16 317.9
1986	14 916.4	14 916.4	135.7	135.7	2 784.0	2 784.0	17 564.7	17 564.7
1987	16 141.3	15 747.6	158.3	154.5	3 153.1	3 076.2	19 136.1	18 669.4
1988	16 673.5	15 641.2	216.4	203.0	3 255.9	3 054.3	19 713.0	18 492.5
1989	17 061.9	15 454.6	420.9	381.2	2 439.7	2 209.9	19 080.7	17 283.3
1990	17 007.9	14 998.2	627.9	553.7	2 397.5	2 114.2	18 777.5	16 558.7
1991	16 575.1	14 277.4	851.9	733.8	2 389.1	2 057.8	18 113.3	15 601.5
1992	17 850.9	15 140.7	982.1	833.0	2 610.2	2 213.9	19 479.0	16 521.7
1993	18 986.0	15 756.0	1 084.7	900.1	2 976.7	2 470.3	20 878.0	17 326.2
1994	N/A	N/A	1 177.5	1 224.8	3 524.7	3 567.2	N/A	N/A

^a Values are in U.S. dollars. For the analytical portion of this document, the values in constant dollars have been converted into Canadian dollars by using the following purchasing power parity indices: 1978 = 1.22, 1979 = 1.23, 1980 = 1.25, 1981 = 1.26, 1982 = 1.29, 1983 = 1.30, 1984 = 1.29, 1985 = 1.28, 1986 = 1.28, 1987 = 1.30, 1988 = 1.31, 1989 = 1.32, 1990 = 1.30, 1991 = 1.29, 1992 = 1.27, 1993 = 1.26 and 1994 = 1.24

^b The trade statistics published by the U.S. Department of Commerce have been restated to conform as much as possible with Statistics Canada classification.

^c Industry shipments less exports and plus imports.

^d At 1986 prices.

Source: U.S. Department of Commerce Catalogue No. MC92-1-25A(P), FT247, FT447 and National Trade Data Bank.

Table 5. Financial Performance

Canadian Household Furniture Manufacturing							
	1982	1983	1984	1985	1986	1987	
Profit margin (%) ^a	0.4	3.2	2.4	2.9	4.0	3.9	
Return on equity (%) ^b	1.4	11.5	8.5	12.5	12.9	10.8	
Canadian Manufacturing Industries							
	1982	1983	1984	1985	1986	1987	
Profit margin (%) ^a	2.0	3.6	5.5	4.7	5.9	6.5	
Return on equity (%) ^b	3.5	6.8	11.1	8.5	10.8	11.0	
Canadian Household Furniture Manufacturing and Wholesaling Industries ^c							
	1988	1989	1990	1991	1992	1993	1994
Profit margin (%) ^a	3.9	3.8	0.3	-1.1	-3.2	0.4	-1.0
Return on equity (%) ^b	10.2	8.2	-8.0	-18.0	-38.6	-3.3	-12.8
All Non-financial Canadian Industries ^d							
	1988	1989	1990	1991	1992	1993	1994
Profit margin (%) ^a	8.6	6.2	4.8	3.5	3.1	3.9	5.3
Return on equity (%) ^b	13.3	10.7	5.0	1.3	-1.0	2.8	7.2

^a Operating profits before taxes divided by operating revenue.

^b Profit after taxes before extraordinary gains (such as gains on sale of assets) divided by total equity.

^c Separate statistics for household furniture manufacturers not available.

^d Separate statistics for all manufacturing industries not available.

Source: Statistics Canada Catalogue No. 61-207 for 1982 to 1987 and unpublished data for 1988 to 1994.

Financial statistics for the U.S. household furniture industry are not available.

Annex B

MORE ON INTERMEDIATE INPUTS

The household furniture industry purchases a large variety of raw materials, components, parts and services. Sawmills provide lumber, while wood product manufacturers supply particleboard and fibreboard. Specialized suppliers provide components and parts, while independent trucking firms supply transportation. While larger furniture manufacturers usually employ full-time designers, smaller manufacturers hire expertise by project. Large manufacturers employ a sales force to serve large buyers and independent agents, often exclusively, to serve smaller accounts. In contrast, the smaller manufacturers primarily use independent agents on a non-exclusive basis.

Solid Wood In North America, solid wood is more widely used in producing a complete piece of furniture than in Europe, where increasingly solid wood is reserved for only the most important applications. Canada imports about 25 percent of required temperate hardwoods, mostly from the northeastern United States, and all tropical hardwoods from Brazil and Central America. Environmental issues are reducing tropical species availability but only about 10 percent of North American furniture production is affected. Softwood (mostly pine) used in 25 percent of furniture production, is relatively plentiful in Canada.

Wood-based Sheet Materials Particleboard and medium density fibreboard (MDF) are cheaper than solid wood, and are expected to be used increasingly. Particleboard shortages in Canada are expected to continue past the year 2000, even when two particleboard plants under construction come on line. In contrast, MDF supplies should not be a problem; by 1997, capacity will increase by 163 percent when two large-capacity mills at Williams Lake, British Columbia, start operation. However, higher standards in North America

than in Europe for board producers may be an issue. Ready-to-assemble (RTA) producers are pressing for lower core densities in particleboards to make them cheaper and lighter in weight. As a hardwood substitute, oriented strandboard and timberstrand are beginning to find favour in the furniture industry.

Upholstery For upholstered furniture makers, fabrics are the single most expensive input and represent about 25 percent of finished product price. The Canadian industry imports about 50 percent of upholstery inputs, primarily from the U.S. and some from Europe. Fashion-oriented furniture producers rely more extensively on imported fabrics. During the 1980s, the Canadian textiles industry rationalized production, narrowing supplier numbers and style ranges, and forcing Canadian producers to increase fabric imports.

Components To reduce labour costs and improve quality, furniture manufacturers worldwide are turning over to specialized firms the production of standardized components (i.e. turnings, drawer sides, mouldings and panels). This growing trend should lead to economies of scale in components supply manufacturing. In 1993, Canadian producers bought about \$64 million worth of components. Sourcing difficulties or delays are not an issue in this industry, although spot shortages can be expected from time to time.

Annex C

MORE ON APPLICABLE TECHNOLOGIES

Hard Technologies

Dramatic developments in “hard” or production process technologies are unlikely in the near future. Instead, research and development by machinery and equipment suppliers will focus on refining current technologies, such as the following.

Computer numeric controlled (CNC) production processes in woodworking reduce setup and loading times and improve quality of cut. The technology was first developed in Europe, where the latest advances are operating. Now made in North America, the cost of these machines is likely to fall, leading to increased use in Canada and the U.S. Another CNC application, using area and linescan cameras, is vision inspection to reduce defects. About 40 percent of Canadian household furniture firms have CNC machines.

Robotics has limited application in furniture manufacturing and is not used extensively in North America or Europe. This technology is primarily used in metal furniture production for welding, frame bending and finishing.

Bar coding has not been fully exploited by either North American or European manufacturers. It can improve efficiency and profitability by allowing each manufacturing centre to feed the following one in an error-free, computer-based, just-in-time process. Less labour and floor space is needed, and accurate labour time accounting and productivity monitoring is possible. It is more applicable to the European use of board materials than to solid timber as typically used in North America.

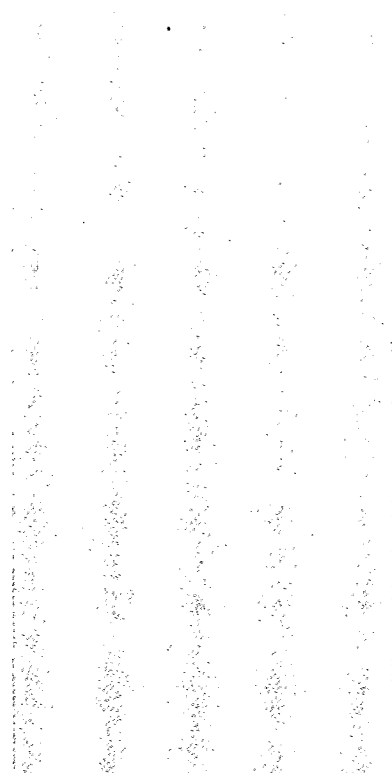
Increasing use of *computer assisted manufacturing* (CAM) systems is expected to integrate production planning and manufacturing processes. In contrast, *computer integrated manufacturing* (CIM), which links and integrates all business functions, will be limited by affordability.

Design technologies, or computer aided design (CAD), in furniture production is at a similar development stage in Canada, the U.S. and Europe. The most important applications are illustration systems to portray design and fabric options in relevant room layouts and thereby allow producers to vary products efficiently and by demand. About 40 percent of Canadian furniture firms have CAD equipment. A link from CAD/CAM to CNC machines may eventually be effective for furniture manufacturers.

Soft Technologies

Just-in-time (JIT) manufacturing systems are designed to respond quickly and efficiently to customer orders through increased flexibility and efficient space use and improved quality. Because customers are demanding increasingly short delivery times and because companies are under pressure to reduce working capital tied up in stock and work-in-progress, introduction of JIT is likely to be one of the most important changes over the next 10 years.

Quality control techniques in furniture manufacturing include incoming material inspection; well-defined operator instructions, machine settings and acceptance criteria; and packer inspection of finished product. More sophisticated measuring devices are intended to prevent rather than correct error. Specialized firm product testing is used and use of formalized standards such as ISO 9000 are increasing.



ISO 9000 is an excellent basis for Total Quality Management, and involves investment in training, understanding internal customer needs, processing inputs, etc. Most furniture manufacturers do not successfully go this extra step to establish formal quality control.

New *marketing technologies* such as furniture viewing and buying via Internet (on-line), by CD-ROM and by TV Home Shopping may be used increasingly in the medium term.

Annex D

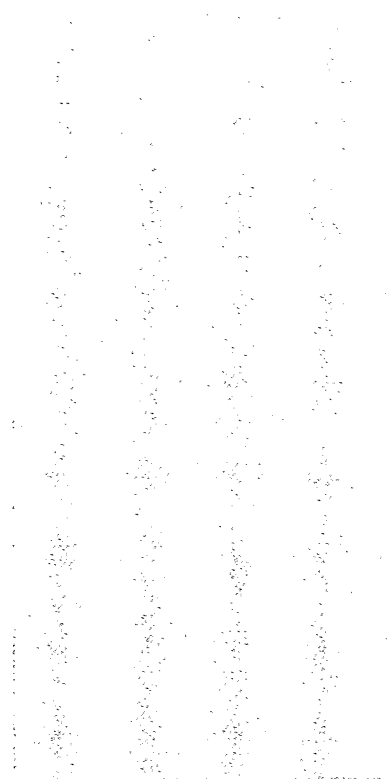
MORE ON DEMAND OUTLOOK

Household furniture competes with other products and services vying for the consumer dollar. As a percentage of all consumer goods and services spending in Canada, personal household furniture expenditures increased from 1.4 percent in 1982 to a high of 1.6 percent in 1988, then declined steadily to a low of 1.2 percent in 1993. Demand is projected to be slower for household furniture than for overall consumer expenditures. As well, furniture demand tends to be highly cyclical, which will test the staying power of producers. In addition to demographic factors, growth may come from pent-up demand due to the recent recession.

Consumer debt as a share of personal income has reached an all-time high. Significant additional borrowings to fuel consumer spending is unlikely.

While household formation is expected to fall from a current annual 190 000 to fewer than 150 000 by 2006, the impact will be at least partially offset by a concentration of new household formation in the over-35 age category, who will have relatively high demands for new dwellings and furnishings. New households buy \$11 000 worth of furniture, compared with \$300 per year for existing households.

The trend toward more varied household types is expected to continue through the 1990s, with traditional family units (opposite sex spouses with children) remaining dominant but continuing to decline. The average household size is also expected to continue to decline, but at a slower rate.



Demographic trends suggest that immigration will supply most of Canada's population growth. Even so, the effect on the household furniture market is not expected to be dramatic, as immigrant taste in furniture is expected to emulate North American fashions. Nevertheless a closer examination of immigrant preference could reveal market niches.

Demand growth will be highest in the large urban centres where population concentration continues. Future household furniture demand will also be influenced by lifestyle and value changes. General consumer interest in home and home products is increasing with the "cocooning" phenomenon. Faced with social, political and economic uncertainty both domestically and globally, the importance of home as a basis for security may increase. In particular, this trend is showing in the growing popularity of home entertainment and shopping.

The home office trend is not expected to increase household furniture purchases; on the contrary, this market may be depressed as office furniture is substituted for traditional household furniture. The numbers of people who can work out of their homes is also limited. Most job growth is in the service areas of the economy, and much of this activity requires personal contact (e.g. health, education) in the workplace.

The "empty nester" trend will not significantly increase furniture expenditures, since increasingly, older people tend to stay in their homes.

Annex E

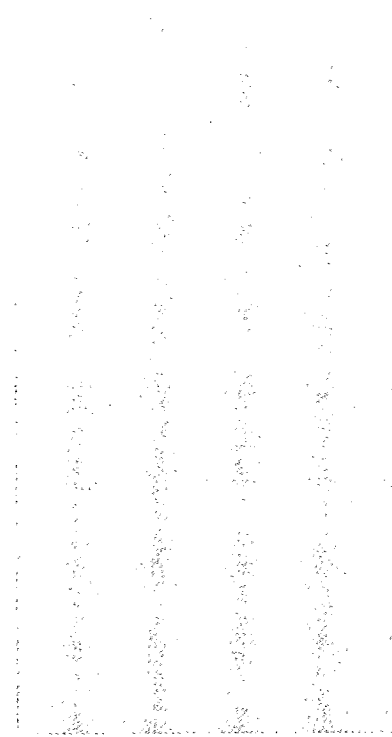
MORE ON RETAILING TRENDS

In 1990, over 3800 retail stores in Canada carried household furniture. While the majority are domestically owned, increased foreign ownership is anticipated. Major retail channels include independent furniture shops (50 percent of outlets), furniture chain stores (20 percent), department stores (10 percent), and warehouse clubs/discount stores (20 percent). Aggressive discounters are gaining prevalence, primarily through underpricing of competitors.

To compete, independents are joining home furnishings buying groups. The largest Canadian group is Groupe Cantrex, a public company based in Saint-Laurent, Quebec, which supplied 728 furniture stores in 1994.

Lifestyle retailing, quick turnaround time and increasing customization are important retail trends. Because the Canadian household furniture market has not yet recovered from the 12-percent drop in sales in 1990, Canadian retailers foresee minimal future demand growth, unless consumer perception of furniture shifts from a price-differentiated commodity to a "fashion" item, resulting in the speeding up of the replacement cycle for new furniture.

Another trend is higher product line specialization with more choices in colour and fabric. Some retailers are adding more value-added, such as decor consultations, to help increase market share. Stores targeting ethnic groups may develop in the largest urban centres. In-store technology, such as



electronic data interchange (EDI) systems and “virtual rooms” (i.e. computerized showcases), will allow consumer choices to be communicated directly to computerized manufacturers.

Since Canadian household furniture producers sell to retailers rather than the public, marketing has been traditionally pitched to retailers, thereby leaving producer image and promotion to them, as well. Retailers also decide the mix of domestic versus imported household furniture to offer consumers. Because retail strategies are at present largely price-based, the success of Canadian producers depends on their cost competitiveness with the U.S.

As part of an Ernst & Young survey (*Today's Challenges Tomorrow's Realities: Towards a Human Resource Strategy in the Canadian Furniture Manufacturing Industry*, 1994), 20 Canadian furniture retailers were interviewed to seek their views on the nature, extent and importance of inter-linkages with Canadian and U.S. manufacturers. Overall, Canadian retailers perceive U.S. suppliers as more innovative, professional and supportive in establishing working relationships than Canadian counterparts.

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