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**REPORT TO
THE PROSPERITY INITIATIVE STEERING GROUP**

"PROSPERITY THROUGH COMPETITIVENESS"

A FISHING INDUSTRY PERSPECTIVE

SUBMITTED BY:

FISH & FISH PRODUCTS SAGIT

D.A. McLean - Chairman

This report has been prepared by a private sector consultation group at the request of the Honourable Michael Wilson, Minister of Industry, Science and Technology and Minister for International Trade as a contribution to the Prosperity Initiative. This document is one of a series of reports setting out the conclusions and recommendations arising from intensive consultations on the competitiveness challenges facing major industry sectors across Canada.



A contribution to the PROSPERITY INITIATIVE

PROSPERITY THROUGH COMPETITIVENESS

A FISHING INDUSTRY PERSPECTIVE

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BACKGROUND

Canadians in all sectors of the seafood industry, harvesting, processing, distribution and marketing, and latterly aquaculture, have always had to cope with the rough and tumble world of international trade. Currently, the Canadian seafood industry is attempting to respond to the emergence of the global economy, and the resultant, increasingly challenging, international trade environment; the industry's success in making the required transformations will determine the future living standards and employment prospects for the country's coastal regions. The need for competitiveness in the industry is as great as in any Canadian industry, and the role of the government in this transformation is critical. Our views on this role are set out in this paper.

Canadian fishermen deliver some 1.4 million tonnes of product annually, making Canada the world 15th largest fishing action. Some 80% of the products manufactured from the fish landed are exported. Nationally, the USA accounts for 60% of exports, Japan 17%, the European Community 15% with the remainder going to over 70 countries. The emergence of the Canadian aquaculture industry in recent years adds to the supply from the "traditional" fishery seeking export markets.

The seafood industry is highly regulated, in harvesting, aquaculture and processing sectors. Many of the regulations, viewed in isolation, seem logical and beneficial, but their cumulative effect contributes to reducing the economic performance of the industry, thus reducing its international competitiveness.

The Atlantic and Pacific costs industries exhibit significant differences. Atlantic Canada is dominated by cod, other groundfish, and shellfish; Pacific Canada's industry is dominated by salmon and herring. The structures of the industries are different, reflecting the stocks, geography and the histories of the two regions. Atlantic Canada relies much more heavily on the US market than does Pacific Canada, to which the European and Japanese markets are the most valuable.

The differences between the coasts naturally gives rise to a domestic fisheries policy that has significant regional variations, to address regional issues and priorities. This paper will refer to some of the critical regional policies that we allege are affecting the competitiveness of the industry on the two coasts. There is, however, agreement between the industries that certain national programs are a restraint on the competitiveness of the industry in both regions.

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We also note that the aquaculture industry in Canada, while still in its infancy, is producing significant revenues and employment for Canadians. However, the aquaculture sector of the seafood industry suffers from many of the same regulatory and policy constraints that the "traditional" industry has experienced. The future competitiveness of all sectors of the seafood industry is not separable by sector, and the recommendations contained in this paper should be construed in this light.

Many governments have struggled with the question of whether the fishing industry in Canada should be a tool of social policy or an industry shaped by economic forces. In the protectionist past, it could be argued that the country could afford the luxury of this debate, and a mix and match set of policies that tried to point the industry in the direction of profitability while maintaining employment in remote communities. The days of affording such luxury in the fishing business are over.

Canada's position as a supplier of fish products is being challenged by many developing countries; Brazil, Mexico, Thailand, Philippines are examples of countries whose fish production is now threatening to surpass that of Canada. Worldwide supplies of aquacultured fish have exploded in the last decade, with serious long term consequences for parts of Canadian industry (most notably BC salmon). Future production from Russia and other republics formerly part of the USSR will find its way to hard currency markets to add to the volumes of fish available, adding to market fluctuations.

NATIONAL FISHERIES POLICY ISSUES

1. THE COST OF MANAGING CANADA'S FISHERY RESOURCES

The industry is concerned about the overall cost to the taxpayer of managing Canada's fisheries. We believe that public expenditures should be carefully directed, and that increased consultation with industry on programs and expenditures is, as a general rule, appropriate.

We have identified three issues which pertain to this matter.

a) DFO Reform

The intent of the Minister of Fisheries and Oceans to introduce legislation to create Atlantic and Pacific fisheries "Agencies" has general support as a concept. The intent to shift the responsibility for the issuing of licences (the fundamental harvest management tool) to a quasi-judicial body, and to have this body act as the enforcement agency for its own rules, makes a good deal of organizational sense.

However, there is a great deal of concern that the Agencies could increase the government's cost of fisheries management, in terms of dollars and human resources.

Recommendation

We believe that the creation of the Agencies should not result in large cost increases. Offsetting reductions should be made in the budget and staff of the Department of Fisheries and Oceans, where possible.

b) Native fisheries and land claims

The government's efforts to address the increasing demands of native peoples for more access to fish is threatening to result in higher management costs to DFO, and to higher costs for the industry. The linkage of Canada's native agenda and the Prosperity Agenda is far from obvious; in fact the two policies are viewed by the industry to be at cross-purposes.

Recommendation

Any native settlements should be tested for consistency with the objective of minimizing government costs, and to ensure that industry competitiveness is not adversely affected.

c) Cost recovery

While we recognize that cost recovery is a policy being applied across government, we find it unsatisfactory that industry is asked to pay the costs of programs over which it has no control and little influence. There is no assessment made by government of ability to pay. Cost recovery, as applied by DFO, seems to focus on generating revenue to cover program costs, rather than reducing and eliminating programs. A recent example of this was the dockside monitoring program in Atlantic Canada. Similarly, in BC, officials focus on how to get industry to generate more than the current \$12 million of revenue, rather than reducing government costs from the current \$150 million closer to the \$12 million revenue.

Recommendation

Cost recovery programs within DFO should be introduced only after broad industry consultation on overall cost reduction, on which programs to make cost recoverable, and the means of raising revenues. Simple justice requires that those who pay the costs must have some direct say in the mix of services provided.

2. POLICIES AFFECTING CORPORATE EFFICIENCY

In Atlantic Canada, groundfish stocks declined between 30 and 60% from 1984 to 1991. Yet in the same period, the number of federally registered fish processing establishments in Atlantic Canada increased by 28% from 724 to 927. This capacity expansion reduced average plant throughput and pushed many operations to being marginal. Profitability and efficiency were sacrificed to the social goal of increasing employment. We have seen in the last two years that such a policy is not sustainable on the basis of pure industry economics, as plants have had to close, only to be reopened with special grants, debt forgiveness and special targeted allocations.

In British Columbia, the fish processing industry became centralized, mainly in the Vancouver area and in Prince Rupert, from the 1930's to the 1970's. The industry benefitted from its own cost reductions. However, we are now seeing growing interest in government to recreate fish processing employment opportunities in remote locations, for social reasons, including addressing aboriginal demands. It is clear that major processing activity in remote locations is only sustainable with continuing public subsidies.

Over-capacities at both harvesting and processing levels continues to be a pressing problem in the industry, whose objective has to be efficiency and competitiveness. Government programs should be working towards having harvesting and processing capacity in line with long term resource availability projections, rather than the current programs that seek short term ways to maintain capacity, and to maximize the number of people who use the industry to access the social network, notably UI benefits.

Over a number of years, industry representatives have noted the lack of consistency in the application of regulations to different firms in the industry. The existence of a regulatory loophole that allows "fishermen-packers" to process fish under less rigorous conditions than a licensed processor is one example of the lack of a "level playing field" under both federal and provincial regulations.

Recommendation

The Federal Government should work to convince the Provinces to implement a moratorium on the issuance of new plant licences for the processing of "traditional" species, and ensure that all licence holders operate under the same conditions. At the same time, policies should provide flexibility for new investments for the processing of aquaculture production.

Governments should not create "artificial" resource programs or financial schemes to keep open plants that have been closed by investors because of shortage of raw material.

3. POLICIES AFFECTING CORPORATE STRATEGIES

Government officials in a variety of Departments which claim the industry as "clients" have little in depth knowledge of the economics of the industry. Many officials who deal with industry programs and policies have little understanding of the relationship of harvesting to processing to competitive marketing. It is simply not enough to believe that the successful husbandry of stocks will deliver economic success at any level of the industry. Fisheries managers must understand that their basic fisheries management decisions can and do affect the financial performance of the industry.

A very current example of how a fisheries manager can affect financial performance can be found in the BC salmon fishery. The world of salmon has been transformed by huge increases in world production and availability of salmon. One response from Canada must be to improve quality, and increase the options available to a processor in how he might treat the incoming raw material.

In BC in 1992, the current fisheries management plan for the Central coast pink salmon fishery does not reflect these new industry requirements. Rather, DFO is planning to manage the fishery in a way that will result in large volumes of fish, some four days old, arriving at the processor. The only production option will be to can the fish. However, the canned pink salmon market is at an all-time low, and is a loss maker for the processor. A relatively simple change in approach would open up new and potentially profitable markets and processing options. Coincidentally, these changes would begin to bring Canadian fisheries management into the same league at that of Alaska, our major competitor in salmon; Alaska has reacted quickly to the changes in salmon markets, and created a competitive advantage for the Alaskan industry.

The Canadian fish processing industry is convinced that fish management and processor policy decisions must be made with a full understanding of the cost implications of those decisions. Progress towards application of the basic tenet that policy should be designed to create a competitive advantage for Canadians is painfully slow, and government officials continue to cling to the notion that larger companies have an unfair advantage that should be redressed by government programs. What is essential is for government programs to provide balance between large and small, between harvester and processors.

A further example of the imposition placed on the industry's competitiveness by Canada's social agenda is found in Atlantic Canada in the area of "developmental fisheries". These fisheries are undertaken with no view to profitability or competitiveness, but simply to show that the government is maximizing harvesting opportunities.

Recommendation

Fisheries policies and production decisions that reflect the old supply driven nature of the industry must be immediately overhauled to reflect the industry's change to a market driven approach.

4. VERTICAL INTEGRATION AND FLEET SEPARATION

The federal government maintains policies that affect the ability of firms to respond to changing markets and trading environments. In British Columbia, there are limitations on the number of licences that may be held by processing corporation; in Atlantic Canada, under the "fleet separation" policy, processors are prevented from vertical integration to the harvesting sector, but harvesters may and do obtain processing licences, thereby increasing shore capacity while reducing fish supplies to existing processors.

Both these policies prevent processing companies from assuring their access to raw materials. They are inconsistent with the Competition Act and must be changed.

Recommendation

Firms in the industry must be permitted to grow to the size that the global economy determines to be efficient, including being allowed to become vertically integrated. Current policies that limit corporate concentration or vertical integration must be swept away. Government must recognize that even the largest Canadian seafood companies are small in global food and seafood terms.

5. UNEMPLOYMENT INSURANCE

The increase in UI premiums in 1991 did not assist Canadian seafood processors to become more competitive. We recognize that every Canadian industry was affected by changes to the UI system, but the harvesting sector of the fishing industry is a very heavy user of the program, and it is doubtful that light users will be prepared to provide income supplements to a seasonal industry for ever.

The Canadian fishing industry is providing seasonal employment in remote areas of the country, in many cases because of government fish allocation programs that are designed to provide these jobs, rather than reasonable market returns. The jobs so created are simply an entry to the UI and welfare network and, therefore, a creation of social policy, not economic forces or a drive to competitiveness.

It is also a fact that fisheries management decisions are being more and more affected by the need to provide sufficient work to participants so that they can qualify for UI benefits. This is a most undesirable feature that will eventually compromise conservation efforts.

Recommendation

The government should conduct an urgent study of possible alternatives to the UI program in the harvesting sector of the fishing industry. This study should review, at least, the possibility of catch insurance programs, and income support and supplements, in keeping with the recommendations of the Forget Commission with respect to fishermen's UI. We suggest that any new study review the Commission's report as a starting point.

THE IMPACT OF NATIONAL ECONOMIC POLICIES ON CANADA'S FISHING INDUSTRY

1. MONETARY POLICY

Given the fishing industry's heavy reliance on export sales, the value of the Canadian dollar is of critical importance. The industry is pleased with the recent decline in the value of the dollar against other major currencies.

The industry knows that it must strive to be competitive at higher dollar values. However, the relatively large swings in the value of the dollar makes business planning very risky in an industry which is already unpredictable because of the buggeries of the resource itself.

The high differential between Canadian and US interest rates penalises the Canadian industry. Most processors work with the banks on operating lines of credit for fish purchases, sales of which may take place some months, and millions of dollars in inventory costs, later. Continued reductions in the real rate of interest would be an important factor in providing the industry with a competitive advantage.

Predictability of the value of the currency is perhaps the critical issue for businesses which must plan in an industry where uncertainty of raw material supply and markets are insecure.

Recommendation

Canada should be working with its G-7 partners towards pegging the dollar within a range of values against a representative, weighted basket of foreign currencies, in a way that parallels the European System.

Efforts to reduce interest rate differentials between Canada and the USA should continue.

2. NATIONAL EDUCATION, TRAINING AND RETRAINING POLICIES

The future prosperity of Canadians is dependent upon the excellence of our education system. That the system has significant weakness has been well documented by the government, and needs not be repeated here. We congratulate the government for its bold identification of the shortcomings of the Canadian education system, and support any and all moves that will lead to improvement.

The implications for the failure of the Canadian education system for this fishing industry are twofold:

- The industry becomes the source of employment for school dropouts
- The industry's needs for trained labour, often in remote locations, are going unfilled.

The industry is pleased with recent government attention to the matters of education and human resources development in the industry, but much remains to be done.

The fishing industry is particularly critical of the lack of attention paid by our education system to foreign language capability. Facility in a second or third language seems to be a penalty in this country, rather than the asset that it should be in helping the industry deal with the international arena in which it operates. We believe that access to other language training should be at least as accessible as is French language training in English Canada.

The fishing industry has for too long been seen as the employer of last resort, from which a person can qualify for UI benefits after the minimum period. The industry supports the notion of tying UI benefits to training requirements, either to upgrade skills in the industry, or as a means of training for alternate employment.

Recommendation

There should be a national focus on language training.

The federal government should work to convince the provinces to make language training a pre-requisite for post-secondary education.

National education standards should be developed forthwith, with federal funding to provinces for post-secondary education contingent on attainment of the national standards.

Changes to the UI program should be made to tie the provision of benefits to becoming more employable ie. through retraining.

3. TRADE POLICY AND PROGRAMS

a) Public sector trade programs

Canada's public support of private sector export efforts is woefully inadequate, in comparison to our major competitors. In many cases, federal and provincial efforts are uncoordinated, resulting in waste and duplication.

The effectiveness of the Program for Export Market Development (PEMD) is constrained by its funding level (in comparison to our major competitors, funding is minor) and by some of the bureaucratic rules that firms must meet.

The Trade Commissioner service is staffed by many dedicated and hard-working individuals. There are many examples where the service has been of assistance to industry. However, the service, from a fishing industry perspective is unfocussed. Many Posts abroad list fish as one of their areas of interest, yet the industry has no interest.

There is, then, an appearance, at least, of Posts justifying programs that are not of much use. It is useless to pretend that a public servant can be closer to a market than a company whose existence depends on marketing. If a company is incapable of understanding the market, it should not be in the game.

Recommendation

Increase the funding of PEMD and organize it so that it can be more easily accessed by companies that could benefit from the assistance.

Ensure that key markets for fish products have Trade Commissioners who are experienced with the industry, or provide them an opportunity to visit and understand the industry.

b) Canadian Trade Policy

The Fish SAGIT supports the government's trade policy efforts in both the NAFTA and MTN arenas, and appreciates the level of consultations that trade negotiators have provided.

We continue to support Canada's position that trade in fish products should be tariff-free, and efforts to address the removal on non-tariff barriers that prevent or reduce Canadian access to foreign markets.

Recommendation

We place a high priority on Canada's efforts to remove tariff and non-tariff barriers that militate against the production of value-added goods in the Canadian seafood industry.

4. TAX INCENTIVES

a) Value-added manufacturing

Many government officials have been critical over the years of the industry's apparent lack of investment in the production of value-added product lines.

It is true that a large proportion of the industry's production is exported as "feedstock" to foreign firms which transform the raw material into products for their own domestic market.

The reason for this is primarily because tariff barriers against final products are significant, eg. EC tariffs against smoked salmon.

The development of new product lines is extremely expensive, often beyond the resources of the relatively small firms in the seafood business. The placing of new products on store shelves, in competition with other food producers who benefit from large scale, year round operations and the existence of supply management, is also a very costly exercise, often beyond the resources of firms in the seafood sector.

b) **Research and Development**

With respect to tax credits for R&D, it is the view of the seafood industry that these credits are far too restrictive. There are no benefits provided to a company which improves its internal efficiency, or invests in productivity improvements. Treatment of investments in manufacturing improvements is also extremely restrictive.

Recommendation

Better taxation incentives are required to encourage the development of value-added products, and the utilization of waste streams, and currently underutilized resources.

The government should re-examine the definition of what R&D programs are eligible for taxation benefits in the fish processing sector.

The government should strive to coordinate R&D programs, and to forge closer partnerships among government, research institutes and private firms in the delivery of R&D.

5. **SUBSIDIES**

Public support, through direct and indirect subsidies, is a pervasive government policy. It consists of cash payments, access for small processing and harvesting companies to specialized government technical consultants, etc., all of which penalise those companies, large and small, which have organized their operations on the basis of the requirement of shareholders to receive an adequate return on investment.

Recommendation

Public subsidies to all sectors of the industry, at both federal and provincial levels, should be withdrawn, and replaced by tax incentives that reward innovation and efficiency.

6. **COMPETITIVENESS REVIEW AGENCY**

It is the view of the Fish SAGIT that the government's commitment to providing a policy and regulatory environment that encourages and rewards competitiveness in the private sector would be given credibility if all government policies and regulatory amendments were subject to a "Competitiveness Review".

We would see this review working in a manner similar to environmental reviews.

Such an Agency would force officials to focus their thinking on the subject of competitiveness, and justify program proposals by demonstrating that they meet the test of competitiveness.

Recommendation

The federal government should consider the establishment of Competitiveness Review Agency, and encourage the provinces to follow suit.

CONCLUSION

The seafood industry is carrying an unfair and intolerable burden in terms of social costs. The industry is treated, through UI, through policies designed to make work for native citizens, as the employer of last resort, and as the entry to Canada's social welfare system. This is unsustainable in the longer term without continuing and increasingly expensive programs of financial support from the federal treasury.

The industry is strapped by policies and attitudes that are outdated and restrain the industry's ability to adapt to the new world and to be competitive.

The government agencies which see the fishing industry as their "clients" must be redirected and organized to obtain a better understanding of markets, production economics, and the dynamics of the international business. Only then will policies be formulated that will help produce a world competitive fishing industry.

The fishing industry cannot be economically efficient if its raison d'être is to be the ticket to Canada's social welfare net, or the vehicle through which native demands are to be met. If, as we believe, the industry cannot provide sustainable employment for the current number of participants, the excess employees and operators must be permitted to fall away from the sector. This may be politically unpopular, but is the only responsible approach.

