

WHAT WE HEARD

The Feasibility of Small Local Meatpacking Plants in Canada

Background

While certain vulnerabilities in the Canadian food system were exposed during COVID, especially in meatpacking where temporary lockdowns occurred when workers became ill, there is general recognition that the system performed remarkably well and continued to deliver safe, consistent high-quality food to Canadians. Questions were raised as to whether Canada's meatpacking industry would have been more resilient if there were more, small, regionally dispersed meatpacking plants across Canada. In an effort to understand this question better, the Canadian Agri-Food Policy Institute (CAPI) commissioned a study on "the Feasibility of Small Local Meatpacking Plants in Canada", with several recommendations for how to improve the sector's resilience.

The paper was the focus of a small invitation-only virtual dialogue on Friday, November 27th organized by CAPI. At this dialogue, a select group of industry stakeholders from federal and provincial governments, industry associations and the meatpacking industry had the opportunity to discuss their views on whether the current structure of the Canadian meat processing industry lends itself to resilience, the factors determining this, and the recommended changes needed to ensure it can be made more resilient in the face of future disruptions. At this dialogue, the author of the paper, Professor James Rude, summarized key findings from his research, followed by a lively dialogue with key stakeholders in attendance.

Key Findings of the Paper

Professor Rude aimed to question what many asserted, that smaller more regionally dispersed plants would have reduced the probability of the spread of COVID-19 and resulted in a more secure meat supply. Major challenges to processors over this period included getting employees to return to work, antitrust complaints against certain processors in the U.S., complaints that the regulators were inflexible and producer complaints about slaughter backlogs. The strongest counterargument to having more small plants is that there are natural forces within the industry that limit slaughter to regions where the livestock is raised and that significant scale (and cost) advantages limit the total number of slaughter plants across North America. He analyzed three scenarios to determine if the sector would have been more resilient under these conditions, including i) if slack were introduced into the production process for major packers, raising their costs, ii) if more robotics were introduced to use less labour, and iii) if there were more small plants. He concluded that a 'one size does not fit all' approach (not "either," "or," but "and") is the answer for future sector resilience and agrees with Temple Grandin of Colorado State University who argues that "(t)he bottom line is, there will always be a trade-off. Big suppliers are low cost, efficient and fragile. More numerous local producers are more high cost and expensive, but the entire supply is more robust with both." (Grandin 2020). Having both structures serve as a risk mitigation strategy.

His second recommendation was that any government support to encourage investment in smaller plants should forego direct government support but rather governments need to create an enhanced investment environment and ensure there are adequate sources of independent market information. His third recommendation was that if slack is to be built into the system, there is a need for an entire supply chain strategy since "(s)upply chain responsiveness is a key dimension of resilience, and future

efforts to enhance resilience through (cooperation), strategic inventory management plans and flexible procurement strategies (along the chain) will be important” (Hobbs, 2020). Finally, a competitive and resilient processing sector depends on open borders and continued integration with the US market. Open borders discipline the use of market power in a concentrated market, incent innovation, and ensure a secure supply of meat when temporary shortages arise.

Key Points Raised During the Dialogue

There is general agreement that a “one-size does not fit all” approach improves resilience

Many participants agreed that **resilient systems** benefit from **diversity** of plant sizes, both small and large, spread across the country. It was suggested that resilience is defined as the ability to continue to supply and offer consistent volume and price regardless of the disruption, from low probability, high risk Black Swan events like the pandemic to higher probability, more frequent disruptions, such as market or trade disruptions. The pandemic was a “people-oriented” disruption since COVID created worker health issues that created the highest risks to meatpacking operations during the pandemic. Several large meatpacking plants were forced to shut down temporarily when plant workers got sick. This is due to the close proximity of workers on production lines and shared accommodation or transportation to and from work. Smaller meatpacking plants also faced this risk but may have had more control over worker safety in small plants and hence experienced little disruption, according to participants. In fact, many small provincial plants experienced surges in demand for their meat products when larger plants were forced to close in late March and early April.

Scale and costs are a key factor determining the prevalence of large, concentrated meatpacking plants in Canada and impact resilience

With representatives from both small and large meatpacking companies in attendance, the dialogue provided first-hand intelligence about the cost pressures facing this highly competitive, low margin industry. **Economies of scale** dominate meatpacking and for this reason it will largely determine any future adjustments that take place in the industry. Large scale plants must operate at high levels of **capacity utilization** to keep costs at a minimum and will have lower unit costs than smaller plants, both because they are larger and can spread their costs over a larger volume, and because they operate at higher capacity. If they want to be more resilient, they would need to operate at lower capacity, and costs would be higher and potentially would be passed on to consumers through higher prices. Larger packers are also best suited to process undifferentiated products because they do not have the flexibility to produce niche products or frequently change product mixes. Without these large commercial plants, Canadian consumers would not have access to the low-priced meat products to which they are accustomed.

On the other hand, smaller packers are best suited to aim for **niche markets** where price premiums can offset higher costs. Some consumers are willing to pay the price premiums associated with local, organic or grass-fed products. In Ontario and Quebec, for example, there is great potential for small and medium meat processors to become global leaders in niche meat products, given the strong agricultural sector, access to fresh water and a huge market of consumers that are willing to pay for niche products. The advantage of small, regional packers for resilience also comes from the fact that the regions in which they operate may have lower COVID caseload infections, and hence have lower risk of closure.

What is important for many small packers is the ability to access export markets or move product interprovincially. This is partly due to the ability to optimize *carcass utilization*, which is also an important consideration for large meatpackers. By boosting carcass utilization through sales of waste streams from the product, meatpackers are able to reduce costs and maximize revenue. Exporting these waste products (e.g. hides) allows both large and small meatpackers to benefit from what would otherwise be a significant cost to them. In addition, the ability of small meatpackers to export niche and specialty products to even a tiny share of the Japanese specialty market, as an example, would provide enormous opportunity for growth and scale-up.

Regulations play a key role in helping or hindering the industry from becoming more resilient

Government officials attending the dialogue explained that *regulations* are in place to ensure that safe, high quality food is available to Canadians and that exported products meet the standards of foreign markets we sell to. However, regulations also boost the cost of doing business, according to industry participants, such as the regulations around Specified Risk Material (SRM) disposal after BSE, which raised meatpackers costs. They also can reduce the ability of the industry to be resilient in the face of disruptions.

Federally-inspected plants have more stringent standards of inspection and food safety in order to meet the requirements of selling into export markets. Provincially-inspected plants, on the other hand, may have less stringent regulations (or be voluntary), which can vary by province in terms of rigour and standards. It is for this reason that only federally-inspected meat is allowed to move interprovincially within Canada. However, during COVID, ministerial exemptions were given that temporarily allowed for the *interprovincial movement* of meat to address regional shortages. This exemption allowed the industry to respond quickly to regional shortages, thereby boosting the sector's resilience. While small meatpackers in some provinces found this advantageous as it boosted their sales and encouraged increased scale, other meatpackers fear that interprovincial movement of provincially-inspected meat may threaten their access to international markets.

The Government of Canada has introduced new legislation called the *Safe Food for Canadians Act* which replaces in large part the *Meat Inspection Act*, enforced by the *Canadian Food Inspection Agency (CFIA)*. Government participants explained how this new act, which was just recently introduced, has in fact attempted to address some of the concerns of industry with regards to flexibility and modernization in how inspections are done and harmonizing standards for provincially-inspected and federally-inspected plants. There is a hope that this new Act will contribute to greater resilience for the industry. COVID has been a test run for the CFIA, where the organization has learned that it is important to also build in redundancy by keeping a back-up list of retired inspectors that can be drawn upon in the event of future disruptions such as another pandemic.

While there was an acknowledgement by participants that the CFIA had been flexible in adjusting certain protocols and processes during COVID to help the industry respond more quickly to COVID's impact, there was criticism of the CFIA relating to the speed of response and more generally in helping exporters meet new standards in certain export markets. This is especially the case relative to the United States where the separation of the Agricultural Marketing Service (AMS) which facilitates meeting new market requirements, from the regulatory arm of the Animal and Plant Health Services (APHIS). Because the CFIA is tasked with doing both, it has been slow to help the industry respond to new market requirements. As an example, it has taken three years to approve what had been in place

for American exporters for 10 years already to meet meat export requirements to the EU. Perhaps a new organization or arm of the CFIA that could provide marketing services rather than just regulating would help industry improve its competitiveness and resilience in the future.

Risks may be best addressed through HACCP-type processes that could be used to boost resilience

Black swan events, such as the current pandemic, are low probability, high risk events that are unpredictable but have major impacts. Industry has to deal with risks in their businesses every day, from trade, market or fire disruptions. To improve resilience, **risk management tools** are essential. There was acknowledgement that as in the case of food safety and animal health risks, processes that bring **HACCP-like critical control points analysis** to bear could help ensure industry will be able to address future disruptions that may be even more drastic or deadly, from animal disease outbreaks, to border closures to future pandemics. One such risk management tool suggested is increased redundancy or slack in the system, as described in Professor Rude's paper. Increased slack would allow meatpacking plants to address the risks associated with worker health and safety, such as during COVID. However, as it would lead to reduced capacity utilization, costs would increase which ultimately may be passed on to consumers through higher prices.

Another effective risk management tool, might be the adoption of robotics, as suggested by Professor Rude, which would reduce the risk of worker health issues by replacing some tasks with robots. Industry participants suggested that robotics are indeed being adopted in some of the larger meatpacking plants and may compliment rather than replace some of the more specialized jobs, such as carcass splitting or analyzing the optimum high quality protein usage from the carcass.

Governments can play a role in helping the industry become more resilient to address future risks

Because robotics and new AI technology require large investments with slow payback, the government could have a role in helping industry match investments such as through matching investment funds for these new technologies, thereby ensuring future resilience. Accompanying this could be programs that support skills training for the more technical workers needed to operate these more complex, new technologies.

After BSE, several government programs were introduced that attempted to subsidize the building of meatpacking plants in Canada to address a lack of domestic capacity that became evident when the border was closed. As Professor Rude argued, very few of these plants ended up surviving or were never built in the first place. Rather than subsidizing the actual building of plants, Professor Rude argues that a better government role might be to improve the investment climate through more competitive tax rates and more efficient fiscal and monetary policies as well as improved market intelligence that can ensure a vibrant, competitive meatpacking industry in Canada that benefits from regionally distributed small and large plants. Also, as was noted by industry participants, market intelligence and information related to the cost of production of pork and beef plants and scale information would serve the industry well. Currently, most of this information is outdated or has been terminated. Finally, the government's role in negotiating free trade agreements and promoting market access is key for a viable, resilient meatpacking industry in Canada. All agreed that open borders and integrated markets with the US as well as access to new emerging markets will help the industry survive and flourish, and prepare them for

future disruptions, which could be even more devastating. This includes promoting multilateralism and the reform of the WTO to ensure that a rules-based trading system will govern future trade and market issues.

Emergency Preparedness for Future Shocks

Finally, if there is one thing that the COVID pandemic has taught us, it is that it is essential to be prepared for future shocks with Emergency Preparedness plans that are up to date and easy to roll out. The slowness with which government responded in declaring agriculture and food processing essential services that needed to be maintained at all costs, was a major source of criticism by industry participants. Government officials acknowledged that COVID was a good test run, and that they had learned how to ensure the industry could continue to deliver safe, consistent supplies of products at reasonable prices during a pandemic. So for example, the CFIA has committed to maintain a list of retired inspectors who can be drawn upon to fill gaps left by inspector workforce shortages. Provincial governments also learned how to address regional shortages of inspectors by cooperating with the CFIA and training and lending provincial inspectors to replace federal inspectors in federally-inspected plants where needed. Industry participants suggested that there could be flexibility allowed at the plant level, which might require pre-approval and training, to allow for plant workers to undertake some of the tasks normally done by CFIA inspectors during emergencies. Certainly, by allowing for digital off-site regulatory approvals during COVID built some flexibility and resilience into the inspection process that could be continued. Finally, there was agreement that greater consultation and cooperation between supply chain partners and government officials could help ensure that industry will be more responsive, nimble and resilient in the face of future disruptions.